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In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 396

FRED M. VINSON, DIRECTOR OF ECONOMIC STABILIZATION, BY CHESTER BOWLES, ADMINISTRATOR, OFFICE OF PRICE ADMINISTRATION, PETITIONER

v.

WASHINGTON GAS LIGHT COMPANY

FRED M. VINSON, DIRECTOR OF ECONOMIC STABILIZATION, BY CHESTER BOWLES, ADMINISTRATOR, OFFICE OF PRICE ADMINISTRATION, PETITIONER

v.

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

CHESTER BOWLES, ADMINISTRATOR, OFFICE OF PRICE ADMINISTRATION, PETITIONER

v.

WASHINGTON GAS LIGHT COMPANY

CHESTER BOWLES, ADMINISTRATOR, OFFICE OF PRICE ADMINISTRATION, PETITIONER

v.

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA

BRIEF FOR THE PETITIONERS

OPINIONS BELOW

The opinion of the Court of Appeals for the District of Columbia (R. II, 428–449) is reported in 137 F. (2d) 547. The opinion of the District Court (R. I, 15–20) is reported in 48 F. Supp. 703.

The opinion of the Public Utilities Commission of the District of Columbia accompanying its order No. 2401 of October 13, 1942, granting a rate increase, is found at R. I, 39–57; the dissenting opinion appears at R. II, 271–317.

JURISDICTION

The judgment of the Court of Appeals for the District of Columbia was entered on July 26, 1943 (R. II, 451). Petition for certiorari was filed on September 29, 1943, and was granted on November 8, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, and Section 43–705 of the District of Columbia Code (1940) being part of the Act of March 4, 1913, 37 Stat. 979, as amended.

QUESTIONS PRESENTED

1. Whether the Public Utilities Commission of the District of Columbia (the "Commission") failed to accord the Economic Stabilization Director (the "Director") and the Price Administrator (the "Administrator") their right to a full and fair hearing under the Act of October 2, 1942 (the "Stabilization Act").

2. Whether the Commission was under a duty, by virtue of its statutory responsibility to establish just and reasonable rates, and in view of the wartime economy and the national stabilization program, to refuse to grant any rate increase in the absence of a clear showing that an increase was necessary.

3. Whether the Commission was under such a duty by virtue of the Stabilization Act.

4. Whether the Washington Gas Light Company (the "company"), which on its own figures was earning a return of 5 percent on a substantially undepreciated rate base after all Federal income and excess-profits taxes, may be held to have made a clear showing that an increase in its rates was necessary.

5. Whether the Commission erred in its treatment of various items of expense, especially (a) the allowance as an operating expense of certain wartime corporate income taxes; and (b) the allowance of depreciation expense on a basis conflicting with that approved in *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U. S. 575.

STATUTES AND ORDERS INVOLVED

Section 1 of the Act of October 2, 1942, c. 578, 56 Stat. 765, 50 U. S. C. App., Supp II, Section 961:

> That in order to aid in the effective prosecution of the war, the President is

authorized and directed, on or before November 1, 1942, to issue a general order stabilizing prices, wages, and salaries, affecting the cost of living; and, except as otherwise provided in this Act, such stabilization shall so far as practicable be on the basis of the levels which existed on September 15, 1942. The President may, except as otherwise provided in this Act, thereafter provide for making adjustments with respect to prices, wages, and salaries, to the extent that he finds necessary to aid in the effective prosecution of the war or to correct gross inequities: *Provided, That no common carrier or other public utility shall make any general increase in its rates or charges which were in effect on September 15, 1942, unless it first gives thirty days notice to the President, or such agency as he may designate, and consents to the timely intervention by such agency before the Federal, State, or municipal authority having jurisdiction to consider such increase.* [Italics added.]

The pertinent provisions of the Emergency Price Control Act, Executive Orders, and the District of Columbia Code, are set forth in the Appendix, *infra*, pp. 98–108.

STATEMENT

1. The Proceedings Before the Commission

On March 20, 1942, the Commission issued Order No. 2219 directing that "an engineering and accounting investigation be made relative to the rates, tolls, charges, tariffs, rules, regulations and

conditions of service of the Washington Gas Light Company, including an investigation in conformity with the sliding-scale arrangement" (R. I, 33) (described *infra,* pp. 9 to 12). On July 21, 1942, the Commission issued a notice under such order for a formal public hearing "in accordance with the sliding scale arrangement established by Order No. 1458" (R. I, 34, 69–73). Hearings were held before the Commission on several days during August and September. At the first hearing a petition of the Administrator for leave to intervene was filed and without objection was granted (R. I, 34–37).

During the hearings counsel for the Administrator repeatedly moved that the basic provisions of the sliding-scale arrangement be re-examined in the light of the price-control legislation and, if necessary, that the scope of the proceedings be broadened to permit such inquiry in order that the true earnings and income of the Company might be ascertained and a determination made whether the Company would be subjected to any undue hardship if required to continue to operate at existing rates. All such motions were denied, on the ground that the issues were limited to the carrying out of the sliding-scale formula established in 1935. The Chairman on September 8 stated that questions pertaining to the basic elements of that arrangement were not within the scope of the proceeding (R. I, 121–123).

By oral and written motions (R. I, 150, 151, R. II, 345–346) the Administrator sought to reopen the proceeding for the purpose of taking evidence with respect to (1) effect of changed economic conditions upon the sliding-scale arrangement, (2) the necessity of revising the sliding-scale arrangement to take account of present economic conditions, "particularly those provisions which relate to rate of return and the allowance of federal income taxes as an operating revenue deduction," (3) effect of the government program to keep down the cost of living upon the arrangement, and (4) all other factors necessary to a proper determination of the justness and reasonableness of the rates of a public utility. The motions were denied by a two-to-one decision of the Commission (R. II, 409).

Thereafter, the Act of October 2, 1942 (*supra*, pp. 3–4; Appendix; *infra*, pp. 99–100), was approved, providing, *inter alia*, for thirty days' notice of utility rate increases to, and consent to intervention by, the President or his agent. October 3, 1942, the President issued Executive Order No. 9250 establishing the Office of Economic Stabilization (7 Fed. Reg. 7871).

On October 13, 1942, prior to notice to the Director, the Commission issued Order No. 2401 approving an increase in gas rates aggregating approximately $200,000, effective September 1, 1942 (R. I, 39–57). One Commissioner dissented

(R. II, 271-317), and concluded that the record justified a large rate reduction (R. II, 316–317). Two days later, the Company served the Director with notice, which did not embody a consent to intervention as required by the Act of October 2, 1942 (R. I, 188–189, 191). The Director, on October 14, 1942, by his Directive No. 1, had designated the Administrator as his representative to receive such notice and to intervene and participate in proceedings upon proposals to increase rates or charges (7 Fed. Reg. 8758).

On October 19, 1942, the Director, by his representative, filed a petition with the Commission praying that Order No. 2401 be vacated, that the proceeding be reopened for the purpose of receiving further evidence and hearing further argument, and that the Director be permitted to intervene and to file a brief in such reopened proceedings (R. I, 57–60). The Commission on October 23, 1942, issued Order No. 2404, which reopened the record "for the purpose of receiving from the Office of Price Administration, on behalf of the Director of Economic Stabilization, additional evidence relating to the inflationary effect, if any, of the increase in rates authorized by Order No. 2401," and intervention was "granted for such purpose" (R. I, 60–63). This order, from the limitations of which one Commissioner dissented (R. II, 317), fixed November 2, 1942, as the date for further hearing. On October 30,

1942, the Company finally consented to intervention by the Director (R. I, 191).

A further petition was thereafter filed on behalf of the Director on October 31, 1942, which alleged, *inter alia,* that Order No. 2404 unnecessarily restricted the Director's right of intervention and improperly limited the type of evidence which the Commission would receive. It further pointed out that in Order No. 2404 the Commission failed either to grant or to deny the prayer of the earlier petition to vacate Order No. 2401 (R. I, 63–65). This petition was denied by an oral ruling of the Commission on November 2, 1942 (R. I, 214–215). One Commissioner dissented from this ruling in a comprehensive opinion (R. II, 322–336).

Hearings were held on November 2 and 4, 1942, devoted chiefly to an effort to secure the withdrawal of the limitations imposed by Order No. 2404. On November 9, 1942, the Commission issued Order No. 2418 denying the petition that Order No. 2401 be vacated, one Commissioner renewing his dissent (R. I, 66–67). Petitions for reconsideration were filed on November 12, 1942, on behalf of the Director and the Administrator setting forth in detail errors in the Commission's procedural rulings and in its determination of just and reasonable rates (R. II, 336–338, 346–353). Both petitions were denied on November 16, 1942, by Commission Orders Nos. 2422 and 2423, one Commissioner dissenting (R. II, 338–339, 353).

Since the hearings were addressed to the sliding-scale formula, an explanation thereof is given at this point.

2. The Sliding-Scale Arrangement

This arrangement was the outgrowth of rate litigation stemming from proceedings instituted by the Commission to bring about a reduction in the gas rates of the company. On March 19, 1935, the Commission entered an order fixing $15,039,000 as the fair value of the undepreciated property of the company as of June 30, 1935. Following further hearings and discussions between representatives of the company and the Commission, the Commission approved the sliding-scale arrangement (Order No. 1458) (Exhibit C, Tr. 258 ff.) as proposed by the company and found it to be in conformity with Paragraph 18 of the Public Utilities Act (Tr. 256 ff.). This Act authorized the company, subject to Commission approval, to provide a sliding scale of rates and dividends. (District of Columbia Code, sec. 43–317, pp. 103–104, *infra.*)

The arrangement prescribed an initial (an undepreciated) rate base of 21 million dollars,[1]

[1] Order No. 1458, Finding No. 2, Section 1, Dec. 13, 1935 (Ex. C, Tr. 256, 261), and Order No. 2682, Nov. 8, 1943, note 17, p. 30, in dissenting opinion; also Transcript in P. U. C. No. 3361, Formal Case No. 334, Aug. 31, 1943, In the Matter of Investigation of rates, tolls, charges, tariffs, rules, regulations, and conditions of service of the Washington Gas Light Company, pp. 61 and 78–91. The rate

and provided that the initial base should be brought up to date, annually, by means of adjustments for net additions to property, less consumers' contributions and less allowances for the proportion of the property used for service outside the District of Columbia. To the property account, an allowance equal to the monthly average of materials and supplies, plus 10% of the annual operating expenses exclusive of taxes and retirement accruals, must be added to give the rate base. (Sections 2 and 3, Order No. 1458, Finding No. 2) (Ex. C, Tr. 258, 262–264, 265). It was further stipulated that the primary rate of return should be 6½% (Section 2D) (Ex. C, Tr. p. 258, 264).

This arrangement also provided a formula by means of which the annual depreciation expense should be calculated (Section 8) (Ex. C, Tr. pp. 258, 266). The annual charge was to be 1¾% of the rate base less the actual earnings of the ac-

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base was taken as $21,000,000, although it was shown at the hearing that this figure was in excess of the reproduction cost new, as of 1932, plus net additions to June 30, 1935, with nothing deducted for depreciation. It was also apparently higher than the original cost new as of the same date. The Commission had found that, as of June 30, 1932, depreciation, to the extent of over $3,000,000, was an existing fact (P. U. C. Order No. 1341, p. 64, (Ex. A, Tr. pp. 124, 191) and No. 1342, p. 13, March 19, 1935 (Ex. B, Tr. pp. 239, 252)). In addition land was still carried, as of June 30, 1943, in the rate base at $821,000 above its original cost (Tr. in P. U. C. No. 3361, Formal Case No. 334, Aug. 31, 1943, p. 17).

cumulated retirement reserve, or less 4% of the average weighted monthly balance of the reserve, if it is not invested outside of the company. This percentage was to continue in effect until the accumulated reserve should exceed 10% of the rate base. As long as the reserve exceeded 10%, the percentage charge used in calculating the annual depreciation was to be 1¼%.

It was also provided that if operating expenditures for production labor, natural gas, other fuels, or taxes, or any one of them, should increase or decrease in excess of 5% of the expenditure in the (previous) test year, then an adjustment in an equal amount should be made in the amount available for return (sec. 6) (Ex. C, Tr. 258, 265, 266).

The plan also provided (Section 2D) (Ex. C, Tr. pp. 258, 264) that, if the rate of return earned should exceed 6½% in any given year, then the revenue should be reduced the following year by certain percentages beginning with 50% of the return earned over and above 6½%. If the return falls to a point above 5½% but not over 6%, then revenues and rates should be increased during the following year by ¾ of the difference between the computed return and 6½%. Where the return falls below 6½%, but not below 6%, no increase is to be made unless the condition continues for two consecutive years. If the return falls to 5½% or below, the amount of increase is ⅚ of the deficiency.

It should be noted that, if the company earns in excess of 6½% in any year, the arrangement does not provide for the taking of any part of that excess income away from the company, but merely for a prospective reduction in the *gross* revenues during the following year. This reduction would never exceed an amount equal to a substantial portion of such *net* income as was in excess of the 6½% in the test year.

Since the company was earning considerably in excess of 6½% on the rate base (Exhibit 12 (R. II, 422) shows it earned 8.5 to 10.6% between 1927 and 1934) the company made a rate reduction of $800,000 on January 1, 1936. It also made prospective reductions of $47,433 on June 30, 1936, $50,492 on June 30, 1938, $163,575 on June 30, 1939, and $63,417 on June 30, 1940, representing 50% or more of the excess earnings during the respective prior years (Exhibit 11, R. II, 421).

3. The Decisions Below

On appeal under section 43–705 of the District Code, *infra*, pp. 105–106, the district court set aside the decision of the Commission, held its action "arbitrary and illegal" and directed that the Commission's Order No. 2401 should be vacated (R. I, 15–21). The court held that the Commission had "regarded the inquiry within narrow limits" (R. I, 18) and "closed its ears to the insistent demand of appellants to give consideration to the new factors required by the act

of October 2, 1942" (R. I, 18). The court ruled that the "right conferred upon the President and his representatives was not a mere formality" (R. I, 19) and "the privilege of intervention is one of substance and has direct relation to the avowed purpose of Congress to stabilize prices, wages and profits" (R. I, 19).

On appeal to the Court of Appeals, that court, Justice Miller dissenting, reversed the district court and sustained the Commission's order. The court held that the right of intervention under the Act of October 2 did not

> * * * confer upon him the power to participate in the decision or to control the proceeding, but merely the right to show that an increase in rates would tend to increase the cost of living and thereby impair the stabilizing effect of the government's price regulation, with the right of appeal where the Commission's action is reviewable by the courts. [R. II, 435.]

The court also held the order could not compel the Commission "to undertake a complete rate investigation against its better judgment much less an investigation upon lines contrary to the governing statute" (R. II, 442). The court apparently held that a fair hearing had been granted and that the Commission was under no obligation to broaden the scope of the inqury.

In his dissenting opinion Justice Miller took the position that Congress intended the Act of

October 2 to qualify the rules of the Commission insofar as it was necessary to accomplish the purposes of the Act. If intervention were limited to a showing that an increase was inflationary, he observed, the Act would be reduced to absurdity. He disagreed with the majority that the only alternative to such an intervention was the power to participate in the decision or to control the proceeding, and he concluded that the argument that a large-scale expensive investigation would be necessary "was advanced by the Commission and supported by the Company as camouflage to hide their unwillingness to permit any inquiry which did not assume and admit the infallibility of the sliding-scale arrangement" (R. II, 446).

SUMMARY OF ARGUMENT

I

The notice-and-intervention procedure established by the Stabilization Act of October 2, 1942, contemplates more than a formal or nominal appearance on behalf of the President's representative. The general objective of the Act was stabilization of the entire economy at September 15, 1942, levels. With respect to utility rates, the existing regulatory agencies were left with jurisdiction over rates, but they are obliged to afford a full and fair hearing to the Administrator as statutory intervenor. (Cf. *Federal Communications Commission* v. *National Broadcasting Co.*,

319 U. S. 239.) Early stages of the present proceeding were brought to the attention of Congress as an illustration of the need for legislation.

A full and fair hearing requires, at a minimum, consideration of data bearing on the true earnings and returns of the utility. Whether such a hearing may be conducted in two parts, the first directed to calculations under an antecedent sliding scale arrangement and the second devoted to a scrutiny of the result to determine whether a genuine need for an increase had been shown, is a question not here involved. The Commission did not grant to petitioners the right to demonstrate the true earnings and returns of the company, holding itself precluded by the sliding scale formula.

II

The Commission has acknowledged that the hearing was conducted under the limitations of the sliding scale arrangement. These limitations were enforced by the rulings on numerous motions and attempts to elicit testimony. Thus an effort was made to show that under a proper sinking fund method of charging depreciation expense, the earnings of the company would be revealed in fact to be more than $225,000 in excess of those stated by the company. This amount would in itself have eliminated the rate increase. Moreover, the Commission refused to consider whether the company was computing its return on a rate base in excess

of original cost. It refused to consider the prospect of increased revenues in the coming year, and the circumstance that revenues during the prior year were abnormally low because of an unusually mild winter. It refused to consider what was a proper rate of return under prevailing wartime conditions, and was content to grant an increase under the sliding scale arrangement even though the company's own figures showed that its earnings were 5% on an undepreciated rate base after all taxes.

The inquiries which the petitioners deemed relevant would not have converted the hearing into a rate proceeding of undue length or complexity. Reproduction cost estimates were not, of course, sought to be introduced. There was an obligation on the Commission, if it deemed the petitioners' requests impracticable in their entirety, to indicate appropriate qualifications. It was not enough that the Commission offered an opportunity to make general representations concerning the inflationary effect of the rate increase which it had approved.

The authority of the Commission to prescribe rules of procedure does not enable it, even under its own governing statute, to abdicate its continuing responsibility to prescribe rates which are just and reasonable. Still less does the rule-making authority justify a denial to petitioners of their statutory right as intervenors to a full and fair hearing.

III

While the petitioners were denied the minimum rights to a hearing under the Act of October 2, it becomes pertinent to consider further the standards which should govern the Commission in passing on a rate increase if the present case is to be remanded. Those standards cannot be divorced from the problem of utility rate increases under a wartime stabilization program. That problem has become one not of preventing sharp and spectacular price rises through selected controls but, as reflected in the Stabilization Act of October 2, 1942, one of avoiding any unnecessary price increases. The duty of the Commission under its own statute to fix just and reasonable rates requires that the canon of necessity be considered. In this view, increases can be deemed just and reasonable only where real hardship is shown, or the company's property is being confiscated, or it is unable to supply additional wartime demands for its service, or unjustifiable discrimination exists.

Under the Stabilization Act itself the Commission, like the petitioners as intervenors, is to be guided by the standard of necessity. It is of no relevance that the President was not given the power to suspend the exemption of public utility rates contained in the Emergency Price Control Act, for, of course, the regulation of utility rates has not been committed to the President or the Price Administrator.

The reliance by the court below on remarks in the Senate to the effect that the intervention procedure would have simply a moral effect gives insufficient weight to the fact that the remarks were made by one who was not completely familiar with the measure as it emerged from conference and who was disappointed that it did not retain the provision which had passed the Senate, giving the President a veto power over utility rate increases.

IV

Even the limited record before the Commission discloses that there was no showing of hardship or of need for a rate increase, and the order may properly be set aside on that ground without remand. A return of 5% on an undepreciated rate base is not so low as to justify a rate increase under the standards applicable in the light of present conditions. The credit position of the company did not require or justify the increase. Its unusually prosperous history and excellent prospects were of far greater weight than its temporary lack of success in floating a stock issue at a time when, as the Commission itself recognized, market conditions were depressed. Nor was the increase justified by reason of the Commission's disallowance as operating expense of income taxes at rates above those in effect for 1941. It was in 1940 that extraordinary emergency and wartime corporate taxation began, and the Commission should have disallowed as operating expense taxes

in excess of the 1939 rates or, if allowing these as expenses, should have made an appropriate downward adjustment in the permitted rate of return. Only thus would the Commission have properly apportioned the burden of wartime taxes.

ARGUMENT

Introductory: Scope of the Issues.—It is our position that, under the Act of October 2, 1942, the petitioners were entitled, as intervenors, to a fair opportunity to demonstrate the true earnings and returns of the company as a condition precedent to the granting of a rate increase. It is submitted, moreover, that such consideration was precluded by the restrictions imposed on the hearing, and that therefore the order of rate increase could not properly be affirmed. These contentions are developed in Points I and II, *infra*. If our conclusion in this regard is sound, the case must, at the least, be remanded for a further hearing before the Commission, as provided in the District of Columbia Code, Section 43–705, *infra*, pp. 105–107. In remanding the case, it becomes appropriate to consider the standards by which the Commission should be governed in passing on the application for an increase. These standards are to be found both in the statutory duty of the Commission to prescribe just and reasonable rates, in the light of wartime conditions and the national stabilization program, and in the Act of October 2. These standards are discussed

in Point III, *infra*. Finally, we shall contend in Point IV, *infra*, that on the limited record before the Commission there was no evidence to justify a rate increase on the basis of these standards and that accordingly the order may be vacated absolutely, pursuant to the section of the Code cited above.

It will be observed that the questions raised do not turn on the mere construction of a local law and are not of limited local importance. Not only are the duties of the Commission under its statute essentially like those of federal rate-making bodies, but those duties cannot be considered apart from the supervening effect of national conditions and national legislation.

I

Under the Stabilization Act of October 2, 1942, the Petitioners Were Entitled, as Intervenors, to a Full and Fair Hearing Before the Commission on Matters Relating to the Earnings and Returns Realized by the Company Which Would Facilitate an Accurate Determination by the Commission of the Company's Need for a Rate Increase

A. The objective of the notice-and-intervention procedure

In establishing the notice-and-intervention procedure as a part of its stabilization machinery, the Congress did not look merely to a formal appear-

ance on behalf of the President. Rather it sought by providing means of effective intervention before regulatory authorities to keep utility rate increases to a minimum, within the purposes of the Stabilization Act of October 2, 1942.

The Act of October 2, 1942, was enacted when the national economy was in jeopardy. Its purpose was to halt the inflationary trends then accelerating[2] and, in particular, to supplement existing controls over commodity prices with new controls over agricultural prices, over wages and salaries, and over common carrier and other public-utility rates. Stabilization of the entire economy at September 15, 1942, levels was its goal.

It is in the light of this objective that the procedure prescribed in the proviso to Section 1 of the Stabilization Act must be viewed. Its requirement that every common carrier and other public utility in the nation give 30 days' notice of

[2] The Senate Committee on Banking and Currency, in its report to accompany S. J. Res. 161 (the Stabilization Bill) 77th Cong., 2d sess. (1942), declared: "The facts presented in the President's message and in testimony before your committee disclose clearly that certain basic factors affecting the cost of living are inadequately controlled in large part because of existing limitations upon administrative powers. In recent months, the economic situation has passed from the critical to the dangerous. There are impending immediately over the horizon such extreme inflationary increases in the cost of living as may jeopardize our entire war program and our economic stability." Sen. Rep. No. 1609, 77th Cong., 2d sess., Sept. 19, 1942, p. 6.

rate increases and consent to intervention by the President's designee was not included in the Act as a perfunctory gesture; the extent to which the problem was the subject of Congressional concern may be measured by the fact that the Senate had adopted a provision giving to the President a veto power over all rate increases. (88 Cong. Rec. 7632.) The conferees' substitution of the notice-and-intervention procedure for the drastic Senate provision reflected, not an unwillingness to stabilize utility rates, but a desire to utilize the existing regulatory agencies for that purpose.[3]

The notice-and-intervention procedure necessarily contemplated the establishment of an office within the Federal Government adequately staffed

[3] See remarks of Congressman Wolcott, a conferee, 88 Cong. Rec. at 7740: "We do not leave utility rates floating around in the air, we leave them under the same jurisdiction they have been under for generations. We have respected the constitutions of the several States, many of which provide that utility rates shall be determined by a utilities commission set up by the people of that State. * * *

"However, we have provided as a substitute for the Norris amendment which we struck from the bill, a provision that the President or any agency that he may designate may intervene in any rate case; 30 days' notice must be given before any rate can be increased, allowing the Price Administrator or anyone else whom the President designates to intervene to protect the public interests, if they do not feel they are sufficiently protected by the utility commissions of the respective States."

The conference report describes the notice-and-intervention provision without discussing it. H. Rep. 2513, 77th Cong., 2d sess., p. 6.

to receive and examine rate increase notices, to determine whether to intervene before the regulatory agencies having jurisdiction, and, where intervention was decided upon, to prepare and present evidence and argument in opposition to the proposed increase, if so desired. Clearly no justification would have existed for setting up this governmental mechanism if the intervention thus implemented were not to be effective intervention. Accordingly, the Court of Appeals was correct in implying the requirement of a "fair hearing" from the terms of the Act requiring the utility's consent to its timely intervention" (R. II, 434–435), since a fair hearing is essential to effective intervention. But neither the Court nor the Commission was justified in allowing limitations to be imposed upon the scope of the hearing when those limitations were inconsistent with effective intervention.

Reinforcement of the view that Congress sought to assure the President's representative a full and fair hearing is found in the legislative history of the Stabilization Act. When Senator Norris introduced his amendment to the Stabilization Bill which, as has been noted, would have granted the President a veto power over utility rate increases, he exemplified the need for such a measure by pointing to the difficulties which the Administrator had been experiencing as intervenor before the Public Utilities Commission of the District of

Columbia in this very case.[4] It cannot be supposed that, in a measure originally designed to put an end to such difficulties, the Congress in actuality merely perpetuated them, and that the Commission's conduct in this case satisfies the requirements of the Stabilization Act. Certainly no such conclusion should be reached unless the statutory language requires it.

Such is not the case. Judge Letts in the District Court and Justice Miller in the Court of Appeals gave a reading to the Act which allows its purposes to be effectuated.

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[4] On September 10, 1942, Senator Norris said, in introducing a bill to confer on the Price Administrator power to veto rate increases (88 Cong. Rec. at p. 7101):

"Mr. President, Mr. Henderson mentions one place where he made an effort to prevent increasing gas rates, namely, in the city of Washington. I think it would not be unfair to say that, figuratively speaking, when Mr. Henderson's representatives appeared before the Utilities Commission here they were politely shown the door. It is true Mr. Henderson has no authority to fix gas rates in the city of Washington, but, as I have said, his representatives were there for the purpose of trying to convince the Commission that an increase in gas rates in the city of Washington meant that all the prices which he had fixed, after investigation, expense, and time, would all be knocked into a cocked hat. As I read the reports in the newspapers, I do not think that the representatives of the Price Administrator were treated with very great respect."

On September 30, 1942, Senator Norris again alluded to this case (88 Cong. Rec. at p. 7878).

Further discussion of the legislative history will be found in Point III, *infra*, pp. 72–77, in connection with the standards to be applied by the commissions in passing on proposed rate increases.

B. THE SCOPE OF INTERVENTION PURSUANT TO THE STABILIZATION ACT

The provision for intervention in the Stabilization Act imposed on the petitioners and on the Commission, respectively, the following duties: It is petitioners' duty as intervenors to bring to the Commission's attention the respects wherein they believe the true earnings and return realized by a utility to be understated in the evidence before the Commission and to raise any other substantial issues pertinent to the question whether the utility is entitled to a rate increase. The Commission's duty to accord the intervenors a full and fair hearing includes the duty to accept and consider relevant evidence proffered by them and, so far as practicable, to determine all substantial issues raised by them relating to the utility's claim to an increased rate.

This statement, we submit, is in accord with the view expressed by Judge Letts and Justice Miller; it is in conflict with the view taken by the majority of the Court of Appeals. Judge Soper derived from the legislative history of the Stabilization Act the conclusion that the Act gave the President's representative "merely the right to show that an increase in rates would tend to increase the cost of living and thereby impair the stabilizing effect of the government's price regulation * * *" (R. II, 435).

The short answer to this view of the Act's effect is Justice Miller's who declared that so

to "limit the effect of the present Act * * * would reduce it to an absurdity. It is a matter of common knowledge that increases in rates tend to increase the cost of living. The Commission might well be expected to take notice of the fact. Intervention and fair hearing would not be necessary to make such a showing. If no more had been intended by the Act it could have been so indicated therein without requirement of notice or intervention" (R. II, 444). He claimed for the intervenors no more—and no less—than the rights of "any other party." He invoked the decision of this Court in *Federal Communications Commission* v. *National Broadcasting Company,* 319 U. S. 239, in which a person entitled by statute to a notice of hearing and authorized to show cause why a license application should not be granted was held entitled to be "afforded opportunity to participate in the hearing, to offer evidence, and to exercise the other rights of a party." (*Ibid*).

More specific guidance as to the duties of the intervenor under the Stabilization Act may be gained from the reasons which lead to intervention in a given case. Not all rate increases are opposed by petitioners, or should be. If, without exception, rate increases were injurious to the national economy, no doubt Congress would have prohibited them flatly, but, just as Congress gave the President authority to authorize necessary adjustments in prices, wages, and salaries above September 15, 1942, levels, and just as the Senate

proviso would have extended his authority to utility rate increases, so the intervention procedure supposes an increase in some utility rates above the September 15, 1942, level.

What standards are appropriate in differentiating between those rate increases which are consistent with the stabilization program and those which are not will be considered in Point III, *infra*, pp. 57–78.

For the purpose of determining the scope of the hearing, it is necessary only to demarcate the range of inquiry. This may be done by noting the extremes. Thus in one case a highly prosperous utility seeks to take advantage of a contract provision for the automatic escalation of its rates; in another case, a utility which has undertaken unusual and unprofitable burdens in meeting war demands, seeks a rate increase when it finds itself unable to meet operating costs out of revenues. Obviously, if any rate increase is to be opposed, it would be the former; if any rate increase is to be tolerated, it would be the latter. What differentiates the two cases, basically, is the difference in the financial situations of the two companies. One has no need for the increase; the other not only is in need but its need is such that its capacity to serve the war effort is imperiled.

Of course, most cases cannot be disposed of so readily. To determine whether a rate increase is

needed usually calls for a "searching investigation," as Judge Letts observed (R. I, 19).[5] If errors in the data or in the legal premises on the basis of which they have been proffered result in an understatement of the Company's earnings or the rate of return yielded by its earnings, what may have seemed an imperative case for a rate increase may be revealed as one where no increase is called for.

Whatever the standards which may be formulated to govern rate increases under a wartime stabilization program, it is clear that they cannot exclude as irrelevant the true earnings and return realized by the utility. These are the basic facts on which informed judgment is to be exercised. To refuse to consider them is to be arbitrary.

It was the duty, therefore, of the Commission, in according a hearing to petitioners in the instant case, to accept and to give careful consideration to such competent evidence as they tendered on matters relating to the earnings and returns realized by the company. Indeed, it was the Commission's duty to determine any substantial issues relating to earnings and return and to the proper rate of return, whether those determinations were based upon evidence offered by the in-

[5] In procedural Regulation No. 11 the Price Administrator has prescribed the data which utilities seeking rate increases are to furnish at the time the statutory notice is given. 7 Fed. Reg. 9390.

tervenors or upon evidence offered by the Company or by the Commission.

The Commission's conduct of the proceedings has been defended during the course of this litigation* on the ground that the Commission has divided the problem before it into two parts: (1) what rates were indicated by the sliding scale arrangement, and (2) whether, if an increase were indicated, it was in conflict with the national stabilization program. With such a plan for the conduct of the proceedings, petitioners would have had no quarrel if the Commission had construed its responsibilities under point 2 to include an inquiry into the actual earnings and return realized by the Company unless it were ready, without such inquiry, to deny a rate increase.

As will be shown in Part II of this brief, the Commission did not so construe its obligation, but instead complained that the intervenors were requiring it to abdicate control over the proceeding. This was not the case. As Justice Miller observed and as will be developed in Part II, there were alternatives open to the Commission which would have enabled it to avoid both the Scylla of a "complete rate investigation" which Judge Soper erroneously insists (R. II, 441) was what intervenors sought and the Charybdis of a hearing confined to the sliding-scale arrange-

*See Brief of Respondent, Washington Gas Light Co., in Opposition to Petition for Writ of Certiorari, at p. 13.

ment. The statute cannot, of course, be supposed to have demanded the administratively impracticable of the Commission, yet it did impose on the Commission the simple obligation of accommodating its procedure to the new responsibilities arising out of the wartime stabilization program.

Release from this obligation is not to be found in the decision of this Court in *Federal Power Commission* v. *Hope Natural Gas Co.*, Nos. 34 and 35, present Term. It was to a quite different point that the opinion of the Court was directed when it said: "* * * It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. The fact that the method employed to reach that result may contain infirmities is not then important." The justice and reasonableness of a rate order cannot be determined unless a hearing has been conducted which has provided a presentation of the relevant facts sufficiently comprehensive to allow those judgments to be drawn. If that has been done, then, as the *Hope* case makes plain, the regulatory authority need not, in obtaining its end result, pursue those intellectual processes which the court may think most appropriate. But if a commission's conclusion is to be reviewed, the court must have access to the facts, and not to an artificial selection from the facts. What this Court

stated in *National Labor Relations Board* v. *Indiana and Michigan Electrical Company,* 318 U. S. 9, 28, is clearly applicable here:

> But courts * * * are granted some discretion to see that the hearings out of which the conclusive findings emanate do not shut off a party's right to produce evidence or conduct cross-examination material to the issue. The statute demands respect for the judgment of the Board as to what the evidence proves. But the court is given discretion to see that before a party's rights are finally foreclosed his case has been fairly heard. Findings cannot be said to have been fairly reached unless material evidence which might impeach, as well as that which will support, its findings, is heard and weighed.

The position of petitioners concerning the right to a full and fair hearing under the Act of October 2, 1942, has recently been sustained by a three-judge court in *Jersey City and Vinson* v. *United States and Hudson & Manhattan Railroad,* decided January 12, 1944 (D. N. J.), wherein the court held this right to have been denied by the Interstate Commerce Commission's refusal to consider evidence offered "to show that the carrier's rise in business and net earnings had completely removed any reason for an increase over the eight-cent fare,"—testimony which in the judgment of the court "went to the heart of the controversy."

II

THE COMMISSION DENIED THE DIRECTOR AND PRICE ADMINISTRATOR A FAIR AND FULL HEARING

A. THE LIMITATIONS IMPOSED BY THE COMMISSION UPON THE HEARING

1. The general rulings of the Commission

The Commission has acknowledged that it limited the scope of the hearing to the sliding scale arrangement. In its brief in opposition to the petition for certiorari (p. 7), the Commission states:

> The statutory order instituting the investigation and the statutory notice did not call for a reexamination, reconsideration and revision of the provisions of the sliding scale. On the contrary, both called for the annual investigation in conformity with the sliding scale arrangement. The Commission refused to change and enlarge the issues and to broaden the scope of the hearings and ruled that the proceeding would be conducted pursuant to the terms of the order and the notice. (R. I, 97, 106, 121-123, 132).

Again, the Commission asserts (*id.* p. 14):

> The Petitioners sought to cause the Commission to review the basic elements of the sliding scale plan and to revise the provisions thereof. This could not be done under the order of investigation or notice of hearing, and to have done so would have been in violation of statutory requirements.

These statements accurately reflect the position of the Commission.[7] But petitioners sought a "revision" only to the extent necessary to determine whether undue hardship would be imposed on the company if required to continue to operate at existing rates. The Commission's narrow view of the case was, of course, consistently urged upon the Commission by counsel for the company during the hearing. When counsel for the Administrator attempted to persuade the Commission that the right of the company to higher charges should be determined by the question whether any undue hardship would result if the company were required to continue to operate at existing rates, counsel for the company not only frankly admitted that the sliding scale arrangement had not operated in such a way as to cause any hardship to the company but contended that the issue was immaterial. Company counsel stated (R. II, 386):

> The first question Mr. Booth mentioned was whether or not the sliding scale has worked a hardship on the Company. There is no such issue in this case. No one claims it has. The question whether it did or did

[7] See also the opinion of the district court (R. I, 17): "Appellants [respondents here] contend that by its rulings and pronouncements it limited its consideration to such data as would enable it to apply the formula of the sliding scale arrangement in determining what rates were authorized by the sliding scale arrangement."

not does not seem to be material in any event. No one is contesting the point.

Both the Director and Administrator made repeated requests that the Commission remove the restrictions on the hearing. These were made both orally and in writing. The Administrator's petition for intervention granted without limitation (R. I, 73) expressly asked for reconsideration of the sliding scale arrangement in the light of the government's stabilization program. On September 14, counsel for the Administrator moved orally (R. I, 151):

> * * * that the Commission issue appropriate orders under which the Commission can in this proceeding give consideration to all relevant facts under which fair and reasonable rates can be determined, by a reconsideration of the sliding scale arrangement in the light of economic conditions which we are now in, in the light of the Government's program to stabilize prices, and in the light of all other factors which the Commission must as a matter of law consider in their determination of fair and reasonable rates.

This motion was taken under consideration (R. I, 151) but no ruling was made on it. On September 28, the Administrator filed a written petition making a similar request, directing attention, *inter alia*, to the question of rate of return and allowance of federal income taxes as operating

expenses.[8]. This petition was denied on September 30 (R. II, 409).

The Commission imposed the same restrictions upon the participation of the Director as were previously imposed upon the Administrator. Both company and Commission have insisted that the Director had no greater right to broaden the scope of the hearing than had the Administrator.[9] Moreover, by the Commission's order of October 23, the Director was restricted to the presentation of "additional evidence relating to the inflationary

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[8] The motion concluded with the following prayer (R. II, 346):

Wherefore, your Petitioner renews said motions and respectfully requests that the Commission issue appropriate orders to:

Reopen this proceeding and direct that further evidence be taken with respect to:

1. The effect of present changed economic conditions upon the provisions of the "sliding-scale arrangement" made in 1935.

2. The necessity for revision of the provisions of the "sliding-scale arrangement" because of present economic conditions, particularly those provisions which relate to rate of return and the allowance of federal income taxes as an operating revenue deduction.

3. The relationship and effect of the Federal Government's program to control inflation and stabilize the cost of living to the "sliding-scale arrangement" and the proceeding.

4. All other factors which are ordinarily necessary to a proper determination of the justness and reasonableness of the rates and charges of a public utility.

[9] The court below held that there was no substantial change in the parties as a result of the passage of the Act of October 2.

effect, if any, of an increase in rates authorized by Order No. 2401, and intervention is granted for such purpose" (R. I, 62–63). During the argument (R. I, 200–208) upon the motion (R. I, 63–65) of the Director asking that the restrictions be eliminated, the Commission was requested to rescind its order of October 13, and to broaden the issues to give the Director an opportunity to demonstrate the true earnings of the company on the basis of proper rate-making principles construed in the light of wartime conditions. The issues of the proper rate base, depreciation expense, war taxes, and fair rate of return were specifically itemized (R. I, 207). These requests were refused by the Commission, as were petitions for reconsideration (R. II, 336–338, 346–353; *id.*, 338–339, 353), one Commissioner dissenting.

That petitioner's requests were administratively practicable and were directed to issues of consequence in the determination of just and reasonable rates under wartime conditions will, we believe, become evident in the following analysis of the Commission's rulings governing specific subjects and of the views of the Court of Appeals with respect thereto.

2. The rulings governing specific subjects.

a. The Commission prevented an inquiry into the additional profits accruing to the company under the sliding-scale method of charging depreciation expense

The Commission denied the right of the Administrator to present evidence, cross-examine witnesses or obtain a determination on the issue whether the Company was securing an additional profit at the expense of its customers by the use of an undepreciated rate base. That the rate base upon which the return of the Company was computed was undepreciated cannot be denied.[10]

We turn to the rulings by the majority of the Commission on this point. An effort was made by cross examination of the Commission's own witness to demonstrate that accrued depreciation was not properly offset by the 4% credit on the depreciation reserve. Cross-examination on these points was restricted by the Chairman, as is shown by the following ruling (R. II, 394; see also *id.* 390):

> Mr. BOOTH. Mr. McElfresh, you indicated earlier in your testimony that the operation of the 4 per cent is intended to provide for accrued depreciation. You do not by that statement mean to imply that it correctly takes care of accrued depreciation in this property in the determination of rates except that * * *. the 4 per cent is merely the proper mathematical calculation under the sliding scale arrangement?
>
> Mr. STEVENS. I object to that question.
>
> * * * * * *

[10] The Commission's opinion in *In re Washington Gas Light Company*, November 8, 1943, states: "Under the provisions of the sliding scale arrangement, the rate of return is applied to an undepreciated rate base" (p. 16).

Chairman FLANAGAN. The objection is sustained. If the questions are confined to the proper calculation made under the sliding-scale arrangement which has been in effect for years, then there is no reason to object to it.

And the Commission prevented the presentation of testimony by the Administrator's witness, a qualified employee of the Federal Power Commission (R. I, 158–159), on this subject when it ruled as follows (R. I, 163–165):

Mr. BOOTH. How did you arrive at the figure of $26,000,000 in Exhibit 8?

Mr. JOSEPH. The $26,000,000 represents my estimate of the maximum amount of depreciable property contained in the rate-base figure of $28,088,332 shown in Column headed P. U. C. Accountants. Materials and supplies, cash working capital and land should be excluded in arriving at the amount of depreciable property. I have estimated that the non-depreciable property contained in the rate base figure of $28,088,322 is equal to at least $2,088,332.

Mr. STEVENS. I move to strike the answer, Mr. Chairman * * *.

Chairman FLANAGAN. I think that motion is well taken.

* * * * *

Chairman FLANAGAN. Mr. Booth, this is so far removed from the limits which I have attempted to impose that I must grant the motion to strike that question with re-

gard to the depreciation. Another factor has now been injected, which is Mr. Joseph's attempt to evaluate this property.

Mr. BOOTH. I think you misunderstand, Mr. Chairman.

* * * * *

Chairman FLANAGAN. Let me clarify one thing. As I understand it, Mr. Joseph, in using the sinking fund method, you have followed what Mr. Booth classifies as the determination made by the Federal Power Commission in the case of Natural Gas Pipeline Company of America; is that true?

Mr. JOSEPH. Yes, sir.

Chairman FLANAGAN. With regard to percentage?

Mr. JOSEPH. With regard to the application of the sinking fund method of depreciation.

Chairman FLANAGAN. Can you mention any points of similarity between the Natural Gas Pipeline Company and the Washington Gas Light Company in the nature of their business?

Mr. JOSEPH. The nature of accounting for both the Natural Gas Pipeline Company of America and the Washington Gas Light Company is precisely the same in that they keep their records under the Federal Power Commission's uniform system of accounts.

Chairman FLANAGAN. But you have not taken the rate of depreciation specifically

set out in the sliding-scale arrangement, have you?

Mr. JOSEPH. I have changed that to conform to the sinking-fund method of depreciation.

Chairman FLANAGAN. I am afraid I shall have to support the motion to strike the answer with respect to depreciation.

And an exhibit containing such a calculation was excluded (R. II, 401):

Chairman FLANAGAN. * * * Exhibit No. 8 is in direct variance with the calculation called for under the sliding-scale arrangement. The method of calculating depreciation is no more correct than a calculation under the direct method would be. For those reasons Exhibit No. 8 is not admitted.

* * * * *

Chairman FLANAGAN. The exhibit is excluded in its entirety.

It is true that following a change of heart upon the part of counsel for the company the majority members of the Commission assented to a suggestion from company counsel that Exhibit 8 be admitted "for whatever weight it may have" (R. II, 403), without waiving the objection to it (*id.* 404). But the decision of the Commission shows clearly that the exhibit (R. II, 420), insofar as it related to depreciation, was not considered by the Commission.

That in thus failing to permit the introduction of the evidence or to give evidence of its consideration, the Commission denied petitioners a full and fair hearing becomes plain when the significance of the evidence is considered. The difference between the proper charge for depreciation expense under the sinking fund method and the charge under the sliding-scale arrangement, as the Administrator's witness attempted but was prevented from demonstrating in Exhibit 8, was over $225,000.[11] *If these figures had been accepted, their acceptance alone would have eliminated the rate increase granted under the sliding-scale arrangement.*

What the Administrator's witness, Mr. Joseph, attempted to do was to demonstrate by the use of the proper sinking-fund method that the application of an interest rate equal to the rate of return resulting in an annual depreciation allowance of approximately $120,000 would still return to the Company's investors over the estimated life of its property their full investment in the Company, whereas the use of a lower interest return, namely 4%, computed on the reserve, resulted in giving to the Company a substantial return over and above the rate of return specifically provided for in the sliding-scale arrangement as the basis upon

[11] The claim under the sliding-scale arrangement was $348,070 and the proper allowance as testified to by Witness Joseph was $120,732.

which rates shall be increased or decreased.[12] As the witness explained (R. I, 161):

> As is shown by the exhibit itself, this amount is that which, if set aside annually for a period of 43 years[13] will, when compounded at an annual interest rate of 6½ per cent equal $26,000,000 [depreciable property shown in the rate base under the sliding scale, R. 163] at the end of the period. * * * In applying the sinking fund method of depreciation it is necessary to use the same sinking fund interest rate as the rate of return. Any lower rate of return would be unfair to the ratepayers; a higher rate of interest, if used in the sinking fund calculation would be unfair to the company.

A further factor indicates the validity of witness Joseph's position as a matter of law. Under

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[12] The position advocated by the Administrator's witness in this case is a basic principle of rate making. See *Report of the Committee on Depreciation, National Association of Railroad and Utility Commissioners* (1943), the summary of which states the following conclusion (p. xix):

> 42. The sinking-fund method may sometimes be used in rate making when it is impracticable to determine the accrued depreciation. When the sinking-fund method is used in rate proceedings, *the interest rate employed should be the same as the rate of return which is applied to the undepreciated rate base.* [Italics supplied.]

[13] The period is derived from the depreciation rate of 2.2 percent used by the company in other connections (see R. I. 162), and is more favorable to the company than would have been the use of the 1.75 percent provided in the sliding-scale.

Section 43–315 of the District Code, *infra*, pp. 102–103, it is provided that the income from moneys in the depreciation fund when invested shall also be carried in the depreciation fund. The company has followed the practice of investing depreciation moneys in its plant. If the property earns a return of 5½, 6 or 7% the statute itself would seem to require that the consumers who provide the depreciation funds be given a credit equal to the return earned by the company on such investments. If this view of the statute is correct, the provision in the sliding-scale agreement calling for the use of a 4% rate is unlawful and must be held inoperative in the determination of proper depreciation expense.

The correctness of witness Joseph's position is established by the decision of this Court in *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U. S. 575, 595–596. There the Federal Power Commission had found that where an undepreciated rate base is adopted as the rate base "unjust enrichment of the companies at the expense of the consumers is a most likely result" unless the interest rate in computing depreciation expense and the rate of return are the same.[14] The Company there claimed that it should be allowed an annual amortization or depreciation charge of $5,100,732, but the use of a higher inter-

[14] See 2 F. P. C. Rep. 218, 230.

est rate and certain other factors resulted in the approval of an annual allowance of but $1,557,582. This Court upheld the Federal Power Commission's action.

In the instant case the Court of Appeals apparently sought to justify the Commission's refusal to consider whether the Company's profits were not in fact some $200,000 higher than as computed under the sliding-scale arrangement by construing this Court's decision in the *Natural Gas Pipeline* case as a principle applicable to a utility of a limited life (R. II, 441) but not to other utilities. The invalidity of that limitation was noted by this Court in *Federal Power Commission* v. *Hope Natural Gas Company,* Nos. 34 and 35, present Term, at p. 10.[15]

Can an end result calling for an increase in rates be valid when the method used in computing the company's depreciation expense conceals a profit to the company greater than the increase which the Commission has found to be necessary? Surely no hearing can be regarded as full or fair in which evidence bearing on so decisive a question is first rejected by the Commission and, when later equivocally admitted, is quite evidently accorded no consideration.

[15] Judge Soper, who wrote the majority opinion in the Court of Appeals in the instant case, joined with Judge Parker in the majority opinion in the *Hope* case, *Federal Power Commission* v. *Hope Natural Gas Company,* 134 F. (2d) 287, in the Circuit Court of Appeals for the Fourth Circuit.

b. The inquiry into the rate base was improperly restricted

The limitations of the hearing also prevented a determination whether the base upon which the rates were computed did not afford the company an unreasonable return, thus placing an undue burden upon the rate payers.

It will be recalled that the rate base under the arrangement was an undepreciated base. Normally, in that situation, a sinking fund method of depreciation accounting is used, whereby it is unnecessary to fix the amount of accrued depreciation, the interest on the accumulating reserve being used to build up the balance. See Barnes, *Economics of Public Utility Regulation* (1942) 267–268, 272. Under the sliding-scale arrangement, however, credit is given at a rate of 4 percent on the depreciation reserve, and it is therefore of critical importance that this reserve shall have been accurately determined. Since the company at least until [redacted] maintained a consistent policy of paying excessive dividends on its common stock instead of providing sufficiently for depreciation expense, its reserve cannot be taken as a proper measure of accrued depreciation.[16] Assuming that Commissioner Hankin has estimated with a substantial degree of accuracy the proper figure to be $5,789,970,[17] the rate payers are being

[16] See note 1, p. 10, *supra;* pp. 87–88, *infra.*

[17] *In re Washington Gas Light Company*, Order No. 2682, November 8, 1943, p. 37.

deprived of an annual credit of approximately $350,000, while receiving a credit of but 4% on a current reserve of approximately $2,300,000, or $92,000. The company is thus being unjustly enriched by over $225,000 for the year.[18]

The rate-base issue raised a further question whether, in determining the right of the company to an increase under wartime conditions, the base should not be limited to the original cost less depreciation, or, at the least, whether consideration should not be given to the fact that the company was obtaining a return on a base over and above the original cost by the use of the sliding-scale rate base. An inquiry into this aspect of the case bore directly upon the issue of hardship between the company's customers and the company. The Commission not only flatly refused this request, but even denied the right of its then Chairman to question a company witness on this issue. (R. I, 96, 97.)

While the Administrator's reasonable request was rejected by the Commission because it limited the hearing to the sliding-scale arrangement, it accepted, without qualification the argument of company counsel that the granting of the request would involve a revaluation and the making of

[18] 6% on $5,500,000 is $330,000. The annual credit on the reserve was about $92,000. Note that the conclusion is borne out in another way by the analysis of witness Joseph. Ex. 8, R. II, 420; see p. 41, *supra*.

reproduction cost appraisals. The Court of Appeals not only fell into the same error but went so far as to conclude that the request of the Administrator on this point was contrary to the Commission's statute because of a provision of the District Act that the Commission shall value the property of every public utility in the District at the fair value at the time of the valuation (Par. 7, *infra* p. 102). Even if Judge Soper's apparent view that "fair value" should be gauged by reference to reproduction cost were still correct, nevertheless neither the statute nor the principles of utility rate making would preclude the Commission from measuring the company's need for a rate increase in an emergency period by reference to the return earned on original cost of its properties.

c. Data as to future operations were not considered

Under the sliding-scale arrangement the determination of the rates is predicated solely upon the past year's operations without any consideration of operations in the future. While the Commission did go outside the record to show in its opinion (R. I, 51) that earnings on the Company's common stock for the year ending July 31, 1942, had fallen, it steadfastly resisted the efforts of counsel for the Administrator to show the improvement in the company's prospects, and both the Commission and the court below, in appraising the company's needs, ignored favorable factors of

demonstrable relevance and importance. To show that improvement in business will offset any need for higher rates which may be indicated by the past year's data is to give recognition and effect to wartime conditions and the exigencies of stabilization.

When, for the purpose of demonstrating that the company's operations were on the upward trend, counsel for the Administrator attempted to obtain access to the company's budget containing its estimates of income and expenses for the full year 1942, the company denied his request (Tr. 821). The budget estimate was particularly important in view of the fact that the Commission staff had accepted a stipulation sponsored by the company's treasurer that no accrual had been made for excess profits taxes in 1942 and that it was not "anticipated that such tax will have to be paid for the current year 1942" (Tr. 808).

The Administrator had contended that upon the basis of the record the company's earnings would continue at such a high level that it would be also subject to an excess profits tax for 1942 and that under those circumstances a rate increase would be clearly inflationary. The Commission ignored this contention and said (R. I, 49):

> The record indicates that the Company will not be liable for excess profits tax for the year 1942.

The error of the Commission's conclusion on this point was admitted by the company in its brief

opposing the granting of the petition in this case."[19]

The Commission failed to consider the fact that the company's own report to its stockholders disclosed that the earnings of the year under consideration would have been larger had it not been for the abnormally mild weather (R. II, 384). This report stated:

> * * * Although some factors other than the temperature variation may have contributed to the diminished use of gas by the average consumer, there is no doubt that if 1941 had been colder, say at the normal average of 45 degrees during the months in which house heating is required, *the gas sales and the earnings of the company would have been larger.* [Italics supplied.]

It has been customary in fixing gas rates to give effect to temperature variations in determining the revenues and income of a gas company for a given year. For example, in *Los Angeles Gas & Electric Corp.* v. *California Railroad Commission,* 289 U. S. 287, this Court sustained the use of average temperature as a basis for a rate reduc-

[19] "In its 1942 order the Commission included a provision to the effect that if any portion of the rate increase should result in the payment of excess profits taxes by the Company, such part of the rate increase should be refunded to the gas customers (R. I, 49). Because of the operation of this provision, early in 1943, the Company refunded to its customers all of the rate increase which was billed between the date on which the rates were put into effect, November 16, 1942, and December 31, 1942." (Brief in opposition, p. 9, n. 11).

tion. If the use of average temperature was proper under peacetime conditions, certainly under wartime conditions an abnormal decline in income due to temperature variation should not constitute the basis of a rate increase.

Moreover, the record also disclosed that the company's revenues for the first seven months of 1942 were approximately $700,000 higher than for the previous year (R. II, 383). Thus, even with the abnormally lighter winter, the increased business of the company enabled it to absorb all cost increases, including higher wages, with the exception of part of the higher federal income taxes payable under the 1942 federal income tax act (Tr. 827–828) if indeed, this increase may properly be considered a "cost increase" (see pp. 89–96, *infra*).

d. The Commission refused to consider what was a proper wartime rate of return

The limitation of the scope of the hearing to the sliding scale arrangement deprived the Director and the Administrator of an opportunity of demonstrating that the rate of return realized by the company was ample. Under the conditions prevailing in 1935 a basic return of 6½% including all taxes may perhaps have been reasonable, if not unduly liberal, for a gas company operating in the District of Columbia. But in 1942 the question was whether a basic return of 6½% after all expenses, including war taxes, was proper in the light of wartime conditions, the stabilization pro-

gram, and wartime sacrifices expected of the nation. This question could not be answered by a mere reference to the arrangement agreed upon in 1935. This Court has recognized changed economic conditions as a vital factor in rate making and in rate of return. (See *United Railways and Electric Company* v. *West* (1929), 280 U. S. 234, 249; *Atchison, Topeka & Santa Fe Railway* v. *United States*, 284 U. S. 248.)

Nor does the argument that the Commission did not in fact allow the Company a full return of 6½% satisfy the obligation of the Commission here. A strong case could be made that a return even of 4% would not be so unreasonably low as to justify a rate increase under wartime conditions (see pp. 80–82, *infra*). Actually, a full hearing would have disclosed that the company was earning more than 6½%.

B. THE COMMISSION AND THE COURT OF APPEALS MISCONSTRUED THE PURPOSE AND NATURE OF THE ADMINISTRATOR'S REQUESTS

The court below reversed the judgment of the district court under the mistaken view that the issue was whether the Commission, as the regulatory body, or the Price Administrator, as intervenor, should control the scope of the investigation. No such issue was involved. The petitioners urged that a further inquiry into the basic elements of the formula approved by the Commission in 1935 was now necessary to determine the pro-

priety of a rate increase, and that such an inquiry would demonstrate the highly relevant fact that the company's profits were substantially greater than as computed by either the company, the Commission's staff or the Commission itself in its order of October 13, 1943.

The court also justified the refusal of the Commission to open up the hearing by envisaging a full-scale rate proceeding of great complexity, involving "laborious calculations and studies" (R. II, 441).

Chairman Flanagan had accepted the argument of company counsel on this point, and in limiting the scope of intervention stated (R. I, 122):

> To question a basic element of the arrangement at this time would undoubtedly result in throwing open all other elements of the arrangement for reconsideration.

We do not concede that it would have been impracticable for the Commission to have carried out all the inquiries specifically requested. If, however, that had been the case, there was an obligation on the Commission to suggest, at least, some reasonable qualifications. There is nothing inherently impracticable in accompanying a determination of rates under the sliding-scale arrangement with an investigation into some or all the aspects of the plan. Indeed, the Commission itself has subsequently deemed it practicable to reconsider the rate of return without reexamining

all other elements in the arrangement.[20] In the light of these considerations and the specific requests made by the Administrator, Justice Miller aptly described as "camouflage" the argument based on asserted administrative impracticability.

The suggestion of the court that the Price Administrator made no definite offer of proof in connection with these matters is also in error. Within the very few weeks that he was in the proceeding, he presented three capable witnesses (R. I, 151, 158, 169). In addition to two technical experts in his employ, the Administrator offered as a witness one of the principal technical experts in the employ of the Federal Power Commission, who had been loaned to the Administrator for the purposes of this proceeding. Had the Commission shown a desire to be assisted by the Administrator, highly qualified witnesses would have been made available.

Of course, the Administrator did not produce "laborious calculations." If by laborious cal-

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[20] See the Commission's Order of April 2, 1943, reading as follows:

"A sliding scale arrangement for fixing rates of the Washington Gas Light Company was established by Order No. 148 of the Commission (Findings Nos. 1 and 2). Under the arrangement, rates are to be adjusted as of September 1 of each year.

"It is ordered:

"SECTION 1. That an engineering and accounting investigation be made, in conformity with the sliding scale arrangement hereinbefore referred to, relative to the rates, tolls,

culations are meant those involved in the hypothetical reproduction cost appraisals incidental to the determination of fair value under *Smyth* v. *Ames*, the Administrator, to be sure, had no such data. But as the record discloses, he possessed substantial evidence dealing with the financial history of the company, with the treatment of war taxes under wartime rate regulation, and with the proper depreciation charge of the company (R. I, 151–178). Practically all such evidence was ignored by the Commission.

The Commission's failure to broaden the scope of its inquiry was attributable to its overestimate of the administrative difficulties arising from the requests of the Administrator. In reversing an order of another administrative agency in a comparable situation, this Court said in *Phelps Dodge Corp.* v. *National Labor Relations Board*, 313 U. S. 177, 198:

> The Board, we believe, overestimates administrative difficulties and underestimates its administrative resourcefulness. Here

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charges, tariffs, rules, regulations, and conditions of service of the Washington Gas Light Company, to become effective on September 1, 1943.

"SECTION 2. *That an investigation be made relative to the rate of return to be allowed the Washington Gas Light Company* on its property used and useful for the convenience of the public, under the provisions of the sliding scale arrangement.

"SECTION 3. That notice be hereby given of the intention of the Commission to hold a public hearing on the subject matter of the investigations." [Italics added.]

again we must avoid the rigidities of an either-or rule.

and at p. 197:

> All we ask of the Board is to give clear indication that it has exercised the discretion with which Congress has empowered it.

C. NEITHER THE PUBLIC UTILITIES ACT NOR THE COMMISSION'S RULES JUSTIFIED THE ARBITRARY LIMITATIONS UPON THE HEARING

The District Act does not support the limitations imposed by the Commission on the hearing. Paragraph 18 of the Act, *infra*, pp. 103–104, authorizing the sliding-scale arrangement, expressly reserves to the Commission continuing regulatory power to make further changes in rates and charges as well as the right to alter and amend all orders relative thereto. This reservation of the Commission's regulatory power was sufficiently broad to encompass the demands of the Administrator (D. C. Code, sec. 43—217):

> The Commission shall ascertain, determine, and order such rates, charges, and regulations and the duration thereof, as may be necessary to give effect to such arrangement, *but the right and power to make such other and further changes in rates, charges, and regulations as the Commission may ascertain and determine to be necessary and reasonable, and the right to alter or amend all orders relative thereto, is reserved and vested in the Commission*

notwithstanding any such arrangement and mutual agreement. [Italics added.]

As the district court held in 1941 in *Potomac Electric Power Company* v. *Public Utilities Commission,* Equity No. 53475, the Commission's duty to fix reasonable rates is a continuing one, notwithstanding a sliding-scale arrangement. The court there held:

> Correspondingly the duty of the Commission is a continuing duty. Neither a court decree nor an agreement can deprive the Commission of that power or absolve it from that duty.

And the Commission has held in connection with the Potomac Electric Power Company sliding-scale arrangement that it "may at any time rectify errors or omissions." [21]

The Commission does have authority by its statute to adopt reasonable rules and regulations governing its hearings (D. C. Code, sec. 43–202). But the power to adopt such rules and regulations does not free the Commission of its dominant responsibility under its statute, as described above, nor can it render meaningless the Act of October 2. The procedural rule-making power cannot be used to justify an increase in rates without adequate consideration of wartime conditions and the relevant data sought to be presented by petitioners, as statutory intervenors. The Commis-

[21] Potomac Electric Power Company, Order No. 2000, February 4, 1941, P. U. C. No. 3261, Formal Case No. 296.

sion is an agency of Congress. It could not adopt regulations which would defeat its obligation to enforce and carry out both its own substantive obligations and those imposed by another act of Congress.

Finally, it should be noted that the Commission actually did go beyond the sliding-scale arrangement. It made an adjustment of federal income taxes in the light of wartime conditions. The Commission was right—as far as it went—in so doing. But the Commission cannot assert its power to make one departure from the sliding-scale arrangement, and at the same time insist that the sliding-scale arrangement precludes it from considering any matters beyond the arrangement's terms.

III

By Virtue of the Commission's Responsibility To Establish Just and Reasonable Rates, and in View of the Wartime Stabilization Program, the Commission Was Under a Duty To Refuse To Grant Any Rate Increase in the Absence of a Clear Showing That the Increase Was Necessary To Relieve Hardship Threatening the Supply of Essential Wartime Services or to Avoid Confiscation. The Commission Was Under a Like Duty by Virtue of the Stabilization Act of October 2, 1942

A. The Problem of Utility Rate Increases in the Stabilization Program

Before the effect of the wartime stabilization program on the standards governing the Commis-

sion's rate-making duties can be appraised, it is necessary to inquire into the economic relation between increases in utility rates and the problem of wartime stabilization. As was conceded in Point I of this brief, not all rate increases are necessarily inconsistent with stabilization. While the financial status of the utility seeking a rate increase was there indicated as significant in discriminating between the inflationary and the noninflationary increase, no effort was made to explore the problem at that point.

It is important to note the special problem which the development of the stabilization program has introduced in the broader problem of inflation control. In the early days of price control, before the enactment of the Price Control Act, the imperative task of the Price Administrator was to stop speculative rises in the prices of commodities under sudden demand,[22] while allowing the orderly readjustment in prices accompanying the conversion of a peacetime into a wartime economy.[23] At such a time the increase

[22] "Actual shortage" was listed 24 times and "heavy forward buying" 10 times in a compilation of major causes of price disturbances among the 33 commodities for which price ceilings had been set as of July 10, 1941. See *The Activities of the Price Stabilization Division and the Office of Price Administration and Civilian Supply*, Hearings before the House Committee on Banking and Currency on H. R. 5479 (Price Control Bill), 77th Cong., 1st Sess. (1941), Pt. 1, p. 277.

[23] "So necessary was the expansion of output to our defense in the period prior to December 7, 1941, and to the

which is inflationary is the sharp, dislocating increase which comes when shortages in supply coincide with intense demand. When, however, the economy approaches capacity production, price can no longer be trusted as an automatic mechanism allocating resources to war needs. Inflationary pressures begin to appear throughout the entire economy, though it may have attained a precarious balance. It then becomes imperative to keep price changes to a minimum. This is the function of a stabilization program.[24]

Naturally, such a program cannot be confined to commodity prices. Those prices influence, and are influenced by, wages and salaries and the rates of common carriers and other public utilities. Moreover, the objective of the program is stability of the economy, not inflexibility of individual prices, rates, and wages. Some prices, some wages, and some rates must be allowed to increase, in the

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successful prosecution of the war since that date, that the Office felt impelled to err in the direction of laxity rather than in the direction of rigor. * * * For the future, economic stabilization requires a more rigorous policy." Office of Price Administration, Third Quarterly Report (for the Period Ended October 31, 1942), pp. 16, 17.

[24] "To stabilize prices in an economy the whole of which is under general inflationary pressure involves holding them steady against any and all increases even though it may not be apparent that such increases have been brought about by inflationary pressure or that they will in their turn tend to increase such pressure upon the prices of other commodities." *Philadelphia Coke Company* v. *Bowles, Price Administration*, Emergency Court of Appeals, No. 47, decided December 15, 1943, pp. 3–4.

interest of obtaining essential production. Failure to relieve such pressures may mean a loss in total national production or losses in certain fields which are important to the war effort. Yet to relieve the tensions, even by minimal price or wage increases, will, of course, tend to accentuate the difficulties of still other producers or, by increasing the cost of living, of still other employee groups.

Since ground must be yielded, it becomes important to yield as little as possible. This means that price, rate, and wage increases must be absorbed whenever and wherever possible. That economic necessity has been stated in terms of legal duty by the Emergency Court of Appeals in an opinion which constitutes a fundamental contribution to the literature of wartime economic control. Responding to the contention that increased coal costs should be transmitted by complainant coke producers to their own customers in the form of higher prices, Judge Maris, writing for the court, said:[25]

> * * * It will unquestionably be necessary for the Administrator in carrying out the enormous task assigned to him to authorize increases here and there in the price structure from time to time as he has done in the case of bituminous coal. These increases may become necessary in order to

[25] *Philadelphia Coke Company* v. *Bowles, Price Administrator, supra*, at pp. 8–9).

> stimulate the production of some commodities in the quantities required by the nation or in order that the price regulations applicable to other commodities may continue to be fair and equitable in the light of changing costs and profits. * * * *Consequently, when such price increases are permitted it is the duty of the Administrator so far as possible to require them to be absorbed at some appropriate intermediate stage in the process of production and distribution at which there may be an existing margin of profit reasonably sufficient to absorb them.* [Italics supplied.]

Perhaps the commonest reason for failure to apprehend this basic proposition is adherence to the criteria applicable during the early stages of price control. Justification for small increases in price which represent only a passing on of cost increases is asserted on the ground that such increases are not "inflationary." To be sure, they are not inflationary in the sense that the skyrocketing price of second-hand machine tools in 1941 was inflationary, but they are destructive of stabilization, and certainly that is inflationary. The fallacy of the thesis that small increases which could have been absorbed are not inflationary has never been more aptly exposed than in the opinion of Chief Judge Vinson of the Emergency Court of Appeals in *Lincoln Savings Bank v. Brown, Price Administrator,* where he said (p. 231):[26]

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[26] 137 F. (2d) 228, decided May 7, 1943.

> A substantial price increase of any commodity will not, in itself, add appreciably to the living costs of the general public. Its weight is milligramic. But the combined effect of millions of these minute quanta, which singly would not shake the scales, could be catastrophic.

It is difficult to believe that the majority of the court below gave full weight to this admonition when it remarked: "Certainly the risk of such inflation as might be expected to follow from an increase of 1/37 of 1 per cent in the cost of living in the District of Columbia was amply justified" (R. II, 438–439). Instead the tenor of its observation accords with that of the Interstate Commerce Commission in authorizing a fare increase for the Hudson & Manhattan Railroad over the protest of the Director and the Administrator who intervened in a suit for injunction instituted by Jersey City. The Commission said:[27]

> It seems to us that an increase of 1 cent in respondent's downtown fare is unlikely to have any inflationary effect, and that the effect thereof upon the cost of living, while a factor to be given consideration, will be so slight, a maximum of about 12 cents a week and 52 cents a month per passenger, as to be negligible.

The Commission's order was enjoined as in disregard of the stabilization program, Judge Mc-

[27] Order of June 8, 1943, 255 I. C. C. 649, 668.

Laughlin, writing for the majority of a statutory three-judge court, quoted this passage and then continued:[28]

> The Commission * * * simply having in mind the small amount in money the increase meant to each passenger taken alone, dismissed this phase of the matter as negligible. We do not see that there was ever any claim by the Director of Economic Stabilization that the raise in rates here by and of itself would result directly in inflation. The gauge urged on behalf of Director Vinson was that set out in *U. S. Gypsum Co.* v. *Brown,* 137 F. 2d, 360, where the United States Emergency Court of Appeals, speaking through Chief Judge Maris said at page 364:
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> "The mere fact that the increase is small and therefore will not bear too hardly upon either party to a sale is of no consequence. It is the cumulative effect of millions of small increases in prices and other costs throughout the economy which starts the inflationary spiral."

If the Price Administrator were to act on the supposition that little risk of inflation is hazarded by increases of $\frac{1}{37}$ of 1 percent in the cost of living, his temptations to yield ground would be

[28] *City of Jersey City, Plaintiff, Vinson, Economic Stabilization Director, and Bowles, Price Administrator, Intervenors* v. *United States Interstate Commerce Commission and Hudson & Manhattan Railroad Co.*, Civil Action No. 3073, U. S. Dist. Ct., N. J., decided January 12, 1944, *supra*, p. 31.

many. Consider, for example, the number of foods included in the Bureau of Labor Statistics Cost of Living Index for the District of Columbia for November 1943, with weights so low that even a 10-percent increase in the price of any one of them would increase the cost of living by less than $\frac{1}{37}$ of 1 percent. There are twenty-two such products: whole wheat bread, rye bread, soda crackers, macaroni, corn meal, rolled oats, veal cutlets, sliced ham, salt pork, pink salmon, bananas, cabbage, onions, canned peaches, canned pineapple, canned green beans, canned corn, dried prunes, tea, shortening (other than lard) in containers, oleomargarine, corn syrup.

Unremitting effort is devoted by the Office of Price Administration to the control of the prices of these commodities. A 10 percent price increase for any one of them would arouse lively concern; no one would take comfort in the thought that the increase raised the cost of living less than $\frac{1}{37}$ of 1 percent. Stabilization is in danger if a different view is allowed to prevail in any other agency which shares in the responsibility for its maintenance.

In the field of utility rates, this danger can be most insidious, for utilities would be the most likely to benefit if tolerance of the small increase went unchecked. In absolute amount, the added charge imposed on each consumer does not seem large, and it is distributed more or less evenly

over the entire year. Since increases must secure the assent of regulatory agencies, they will be most frequently sought in amounts which, percentagewise at least, are small. But the cumulative effect of such increases in utility rates may be serious. The aggregate gross revenues of the electric light and power companies and gas companies constituted $3,850,000,000[29] in 1942, and this total has been exceeded in 1943. Applied to the 1942 revenues, an increase of only five percent would amount to nearly two hundred million dollars. A great many million more could be added if the calculation were extended to telephone, water and heat companies, and to common carriers.[30] Furthermore, these figures disregard increases in the prices of other commodities and

[29] Source: for electric light and power and manufactured gas: Moody's Public Utility Manual for 1943; for natural gas: Survey of Current Business, U. S. Department of Commerce (1943).

[30] The problem of common carrier rate increases remains a real one, despite the unprecedented profits of the railroads. Although the carriers did not take advantage of the Interstate Commerce Commission's order of October 7, 1943, to show cause why the suspension of the 1942 rate increase of 6% should not be extended through June 1944, still it must be remembered that, influenced by the view that the rail carriers are entitled to recoup their depression losses in wartime, five of the eleven members of the Commission voted against the suspension when it was ordered in April 1943 (*Ex parte No. 148, Increased Railway Rates, Fares, and Charges, 1942*, 255 I. C. C. 357). Moreover, a significant proportion of the thousands of notices of carrier rate increases received by the Administrator come from rail carriers.

services to which increases in utility rates contribute.

B. THE COMMISSION'S DUTY TO FIX JUST AND REASONABLE RATES UNDER THE PUBLIC UTILITIES ACT

If the analysis of the problem of utility rate increases in the stabilization program is accepted, it becomes clear that the effectuation of that program requires the denial of all unnecessary rate increases. Since, by the statute declaring its power, the Commission may fix only just and reasonable rates,[31] it would constitute an error of law for it to authorize an unnecessary increase in an existing rate which is not shown to be unjust or unreasonably low.

In Point IV, *infra*, pp. 78–96, the question will be considered whether there was substantial evidence of record to sustain a finding that the rate increase the Commission ordered was necessary. But before that inquiry is undertaken, further consideration must be devoted to what may possibly seem a severe conception of the Commission's wartime legal duty.

The canon of necessity is a strict one. In all but exceptional cases, necessity can be found only where real hardship is shown. If a company is threatened by inability to maintain needed service, or if, despite a recognition of wartime exigencies, a court would be forced to conclude that

[31] District of Columbia Code (1940 ed.), §§ 43–301, 43–414. *infra*, pp. 102, 104–105.

the company's property is being confiscated, or if a company, though able to maintain existing services, is too hard pressed financially to be able to supply added wartime demands for its service, necessity properly may be found. And, since discrimination is incompatible with the basic obligation of the public utility, necessity for an increase may be found in those infrequent cases where an unjustifiable discrimination cannot be corrected by reducing the higher rate.

While the criterion of necessity may be susceptible of still further refinement, petitioners submit that the most effective formulation is that to be derived from the Act of October 2 itself. In describing the circumstances in which the President may adjust prices and wages stabilized at September 15 levels, Section 1 declares that he may do so only "where necessary to aid in the effective prosecution of the war or to correct gross inequities." The very applicability of those statutory standards to virtually all prices of commodities and services and to wages and salaries reinforces both the importance and the justice of recognizing that like standards inhere in the concept of just and reasonable rates in wartime.

The justice of applying the same standards to utilities becomes all the more evident when note is taken of the fact that utilities are peculiarly the beneficiaries of successful stabilization. This fact is convincingly attested by the plight of the utili-

ties during and immediately following the First World War.[32] In 1917 and 1918 there was sharp and sudden rise in the prices of commodities and services which the utilities had to buy. In particular, the cost of oil, coal, and labor soared. The situation became critical; the War Finance Corporation, the chief source of capital, was embarrassed by its inability to lend upon the inadequate security afforded by utilities unable to earn enough to pay fixed charges, taxes, maintenance, and repairs. The Secretary of the Treasury in a letter to the President dated February 15, 1918, stated that many public utilities needed prompt help, and the President in reply endorsed this position.

Appeals by distressed utilities to regulatory authorities for emergency aid were many. This was generally given, after the usual lag, but it is of interest to note that the rate of return allowed was not the normal one. Examples of this position are numerous. Thus the Supreme Court of Utah declared:[33]

> It is therefore of the utmost importance that the commission should proceed with great care in changing rates. While caution in that regard should be exercised, yet at this time, when the whole world is en-

[32] The report of World War I experience in the text is derived from *In re Empire Gas & Electric Co.*, PUR 1918D 916–17 (N. Y. P. S. Comm. 1918).

[33] *Salt Lake City* v. *Utah Light & Traction Co.*, 52 Utah 210, 228–229, 173 Pac. 556 (1918).

> gaged in a most destructive war and every condition is grossly abnormal, to do so is of special importance. While, generally speaking, every utility that serves the public must be allowed a fair and reasonable return on its investments over and above the actual cost and expense of providing adequate, efficient, and safe service when economically managed, yet it is not true that such a return must be assured to every utility when, as now, the conditions are grossly abnormal on account of the war and while such conditions are necessarily temporary.

And in granting an emergency increase the New York Commission said:[34]

> This certainly will not yield as large a return as might be reasonably expected in normal times. * * * We think, however, that the public-service corporations must and do expect to submit to their share of the common sacrifice and that neither the appeal of President Wilson nor the ruling of the War Finance Corporation had in view the maintenance in all cases of normal profits.

The contrast is marked between the distress that was endemic among utilities in the previous war

[34] See note 32, page 68, *supra*. Similar views were expressed in several other cases involving war emergency rate increases necessitated by the inflation in prices then occurring. *Smith* v. *Railroad Commission*, PUR 1918C 577 (Cir. Ct. Wis. 1918); *In re Queensboro Gas Co.*, PUR 1918C 872 (N. Y. P. S. C. 1918).

because of inflationary price rises, and the stability of all, and the prosperity of most, public utilities which prevails today. To require utilities to absorb the modest cost increases which must continue despite price and wage controls is to require them to take out inexpensive insurance against the upward sweep of costs which would follow if those controls collapsed.

Even though these considerations may be accepted as appropriate when addressed to the discretion of the Commission, it may be argued that they give rise to no legal duty from which departure may be corrected by a court. But this Court recognizes judicial authority to scrutinize the "total effect" of the "result reached" by commission action,[35] and, of course, the courts remain charged with the function of statutory construction. Petitioners believe that the Court will find no difficulty in characterizing as unlawful the result reached by the Commission's action in this case, once the Court has construed the standards embodied in the District of Columbia statute so as to give effect to the governmental objective now dominant: economic stabilization. This task is one which the Court is peculiarly fitted to perform. A

[35] "Under the statutory standard of 'just and reasonable' it is the result reached, not the method employed which is controlling. * * * If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end." *Federal Power Commission* v. *Hope Natural Gas Co.*, Nos. 34 and 35, at pp. 7, 8.

commission may be expert in balancing the conflicting interests of consumers and investors, but where a governmental interest transcending both those interests comes within the orbit of a commission's responsibilities, it is the judiciary which, as arbiter, must determine whether the emergence of that interest shall operate to contract the area of commission discretion.

The effect of the enactment of the Emergency Price Control Act, and especially of the Stabilization Act, is to oblige the Commission and all rate-making agencies to make a "careful accommodation of one statutory scheme to another". In such a situation, the Court remarked in *Southern S. S. Co.* v. *National Labor Relations Board*, 316 U. S. 31, 47, "it is not too much to demand of an administrative body that it undertake this accommodation without excessive emphasis upon its immediate task." All the more is this true when the effect of the supervening legislation is to establish the basic economic conditions with reference to which the Commission ought properly to discharge its own statutory function.

In one respect, to be sure, the problem is a novel one. Characteristically, controversy in rate cases has centered on the question whether the rate is too low, and the disputants have been commissions and companies. In the infrequent situations where the consumer interest has been represented by spokesmen other than the regulatory

agencies, some courts have been hesitant to give relief. But no reasons for such hesitancy exist in this case. Here the rule would be clear-cut; if no unnecessary increase is lawful, there is no "range of reasonableness" to delimit. The interest involved is a national interest of a grave emergency character, represented in the proceedings by a duly authorized Federal agency, distinct from the local consumer interest normally represented by the municipality or regulatory authority itself. Hence the instant case does not require the Court to anticipate such problems as may spring from judicial review of administrative action at the suit of a consumer.

C. THE COMMISSION'S DUTY UNDER THE STABILIZATION ACT TO DENY UNNECESSARY RATE INCREASES

In the preceding section attention was focused upon the effect of the wartime stabilization program on the Commission's obligation under its own statute to establish just and reasonable rates. When the problem is so conceived, the Stabilization Act is important as a dominating factor in the wartime economy within which the Commission is required to act.

But the duty of the Commission to give full effect to the stabilization program need not, we submit, be derived solely by adapting the concept of just and reasonable rates to wartime conditions. The government of the nation has, in the

exercise of its war powers, adopted stabilization as its wartime economic policy. By Congressional enactment, implemented by Presidential order, it has in effect directed the stabilization of cost-of-living prices, wages, and salaries, and of common carrier and other public utility rates at September 15, 1942, levels, subject to adjustment by the President or his delegate in the case of prices, wages, and salaries, and by the regulatory authorities having jurisdiction in the case of utility rates. The question then arises whether, in thus entrusting the responsibility of rate stabilization to the regulatory authorities, the Stabilization Act itself placed them under a legal duty not to authorize unnecessary rate increases contrary to the interests of stabilization.

The consideration of this question has been confused by the fabrication and subsequent annihilation of a man of straw. It has been urged that the Congress intended to place no legal duty upon regulatory authorities by adopting the Stabilization Act (other than the duty to accord the President's representative a fair hearing) because the Act (section 2) does not confer on the President the power to suspend the provision in the Emergency Price Control Act excepting utility rates from regulation thereunder.

What seems to have been the source of the confusion is a provision which accompanied the Norris Amendment when it was adopted by the

Senate.[36] Because the President might wish to exercise the power to veto utility rate increases by delegating authority to the Administrator to proceed under the Emergency Price Control Act, he was granted authority to suspend the provision in that Act forbidding the regulation of utility rates. The President's power to control wages was accompanied by a like power to suspend the provision exempting wage rates from the Price Control Act. When, however, the Norris Amendment was rejected in conference and the notice-and-intervention procedure substituted, there was no longer any reason for the President to be given power to suspend the provisions exempting utility rates from regulation under the Emergency Price Control Act. Accordingly, the power of suspension was dropped and the exemption clause was preserved intact.

We concede that neither the President, nor his delegate, the Director, nor indeed the Administrator, has any authority to regulate utility rates under the Emergency Price Control Act or the Stabilization Act. At no time has this been attempted. Surely to appear as intervenors before a regulatory authority having jurisdiction over utility rates to contend that conformity to the Stabilization Act requires the regulatory authority to deny

[36] For the text of the bill as passed by the Senate, see 88 Cong. Rec. 7719. The provision in question appeared in section 2.

unnecessary rate increases does not make the intervenors the regulators of the rates in question.

Quite different is the question whether the Stabilization Act imposed a duty on regulatory authorities. The Act does not do so explicitly; the legislative history is not decisive; and the answer must be found by a consideration of what the Act did provide and why it did so.

Did the Act necessitate the establishment of governmental machinery for the receipt of notices of rate increases, for their consideration, and for the intervention by the President's representatives before regulatory authorities, only in order to create a sense of moral discomfiture in the latter bodies if they acted in disregard of the demands of stabilization? Such is the conception of the Act's purpose which was urged by the Commission and the Company and which was accepted unqualifiedly by the majority of the Court of Appeals. Its basis seems to be rooted in the remarks of Senator Norris on the floor of the Senate when the conference report rejecting his amendment was announced by Senator Brown.

Senator Norris was disappointed. When he said that intervention would have a "moral effect," [37] he was not expressing a view derived from any extended analysis of the substitute measure, but rather was intermingling disparagement and praise in the way of one who is deciding to make

[37] 88 Cong. Rec. 7723 (Oct. 2, 1942).

the best of an unsatisfactory compromise. His incomplete apprecation of the effect of the substitute measure is revealed by his assumption that the President's representative as intervenor would have no right to appeal an adverse decision. When Senator Brown promptly corrected this misconception, Senator Norris conceded that this "would add a great deal to the legal effect of the language which has been placed in the measure."[38]

We believe the right of appeal does indeed add a great deal to the Act, for we submit that it is a right to challenge the order of a commission which has disregarded its responsibilities under the Stabilization Act as well as its duties under its local public-utilities law.

Support for the view that Congress expected regulatory agencies to be subject to the same legal standards in passing upon rate increases as the President would be in passing upon price and wage increases is to be found in the history of the relevant provisions. The amendment introduced by Senator Norris took the form of a proviso appended to the second sentence of Section 1, which gives to the President power to adjust prices and wages over September 15 levels and which specifies as the standard to govern his action that it be "necessary to aid in the effective prosecution of the war or to correct gross inequities." However, the proviso giving him power to veto utility

[38] *Id.* at 7723.

rate increases over September 15 levels contained no standards. This was natural; the proviso merely introduced an additional subject matter, utility rates, and prescribed a different procedure, review of commission action. But the President's action under it, in permitting or vetoing rate increases, would surely be subject to the standards prescribed in the same sentence to govern his action in adjusting prices and wages.

When the conferees came to change the procedure thus provided, there was still no occasion to provide other standards. The standards to govern the President's representative in intervening would, of course, continue to be those which would have governed the President in vetoing rate increases, and, for the same reason, the same standards would be applicable to the regulatory authority which, free from the President's veto, was entrusted by the proviso with the responsibility of determining whether to allow increases in rates over September 15 levels. That the final authority was reposed in the regulatory body rather than in the President does not mean that its exercise was to be free from legal responsibility to conform to the requirements of stabilization.

That the Stabilization Act did impose a substantive obligation upon the Commission is the view of the majority of the statutory three-judge court which has recently issued a permanent in-

junction restraining the Hudson & Manhattan Railroad from putting into effect an increase in certain of its fares which had been authorized by the Interstate Commerce Commission over the objection of Jersey City and of the Director and the Administrator,[39] and repudiating the Commission's view that the increase, being small, was "unlikely to have any inflationary effect."[40]

IV

The Record Before the Commission Discloses that There Was No Need for a Rate Increase and the Order Should Have Been Set Aside on that Ground

A. The Limited Record Before the Commission Discloses that the Company's Return Was Adequate If Not Unduly Liberal in the Light of Wartime Conditions and Did Not Justify the Increase

The record before the Commission, as we have demonstrated, was incomplete, and for that reason its order could not properly be affirmed. By its restrictive rulings, the Commission precluded itself from determining the real earnings of the company or from adequately considering the relative equities of the company's consumers and investors. In addition, we submit that there was no evidence in the record upon which the Commission could have concluded that the company would be subjected to hardship or that its return

[39] *Jersey City* v. *Hudson & Manhattan R. R.*, *supra*, p. 63.
[40] See 255 I. C. C. 649, 663.

would be unreasonably low if required to continue to operate at existing rates.

The principal exhibit of the three offered by the company was exhibit No. 2 (R. I, 233–234), comparing the computations by the company's and the commission's accountants of net amount available for return. The exhibit disclosed that the net operating income as computed by the company after all expenses including all federal income and excess profits taxes was $1,366,119, or 4.87% on the sliding scale rate base. The total federal income and excess profits taxes included in the expenses by the company were $526,440. Since this was computed prior to final enactment of the Revenue Act of 1942, a subsequent computation disclosed that the revenue act as finally adopted by Congress would reduce this liability on an annual basis by $36,000 (R. I, 223–226). This item served to increase the company's net income after all expenses to approximately $1,400,000, or 5% on the undepreciated rate base.[41] It should be noted that both the Commission and the court below ignored this saving to the company, for both assumed the return on the company's figures to be 4.87%.

Exhibit 8, offered by the Administrator, first excluded by the Commission and then equivocally

[41] This increased the company's return from 4.87% to 5% for the same period, since .13% of the rate base ($28,088,332) (R. II, 420) is approximately $36,000.

admitted (*supra*, p. 40), indicated that by giving effect to the sliding-scale arrangement and making two adjustments in the company's expenses, one relating to depreciation expense and one for income taxes, the company earned a profit of $95,335 for the sliding-scale year ending June 30, 1942, over the 6½% basic return provided for in the arrangement and that, therefore, a rate reduction of half the excess, or $47,668, should have been ordered pursuant to the arrangement itself. Commissioner Hankin in his dissenting opinion, after giving effect to these and other factors, concluded that a rate reduction of approximately $1,000,000 was justified (R. II, 271, 316-317).

A return of 5% on an undepreciated rate base, it must be clear, could not produce a return which was so unreasonably low as to warrant a rate increase under wartime conditions. This Court in 1940 held that no substantial federal question was presented by a decision which held that a gas company was not suffering confiscation where its rates yielded a 5% return (*Peoples Gas Light and Coke Company* v. *Hart*, 309 U. S. 634). Such a return allowed only peacetime income taxes and did not take into consideration the reduction in return which would be justified under wartime conditions by the inclusion of all federal income and excess profits as an operating cost. In *West* v. *Chesa-*

peake and Potomac Telephone Company, 295 U. S. 662, 683, three members of this Court stated:

> There is at least grave doubt whether a return of 4½% is so out of line with the current yield on invested capital as to be deemed confiscatory. This doubt, if accepted principles be applied, must be resolved against the company, which has offered no evidence by which the doubt could be removed. Twenty-five years ago, in times far more prosperous than these, this Court unanimously declined to take judicial notice that an estimated net return of 4% would be confiscatory *Knoxville* v. *Knoxville Water Co.,* 212 U. S. 1, 17.

The earnings of the company are considerably higher than have justified rate increases granted by other regulatory commissions. Two cases involving gas distributing companies are pertinent. In both, rate increases were denied though the utilities were earning a lower rate of return than might be considered reasonable under wartime conditions. In the *Dedham and Hyde Park Gas and Electric Company* case, 48 P. U. R. (N. S.) 257, 260, the Massachusetts Department of Public Utilities on May 17, 1943, refused an increase in rates though it appeared that the company was earnings about 3½% on its net investment. The company's financial history and current position were extremely unfavorable compared to the liberal earnings of the Washington Gas Light Company.

And the Public Service Commission of Kentucky, in the *Western Kentucky Gas Company* case, where the company contended that it had been earning only 1½% on its net investment, denied the increase in the interest of the stabilization program, holding (— P. U. R. —):

> In normal times the record made by applicant might entitle it to favorable consideration. That we do not now decide. However, times are not normal. A war emergency exists that affects the whole nation; and we do not believe that, under existing circumstances and the expressed policy of the Federal Government, an increase should be allowed in utility rates unless and until it is shown to this Commission that service to the consumer would be impaired. This record does not affirmatively or otherwise show that the service furnished to the consumer would be impaired if the application is not granted.

As we have shown, the earnings of the company in the present case were understated. Moreover, the company's increased revenues had offset by the time of the hearing in 1942 all increased operating costs with the exception of part of its higher federal income taxes, and it had every prospect of higher net income in the coming year. See pp. 49–50, *supra*.

B. THE CREDIT POSITION OF THE COMPANY DID NOT JUSTIFY THE INCREASE

After a review of the company's current financial position (R. I, 50–51) the Commission concluded that its "credit position * * * depends in large part upon the integrity of this Commission in administering the sliding scale arrangement" and that the rate increase of $201,424.74 should be authorized. This increase the Commission stated will "tend to arrest the decline [in earnings on the common stock] and preserve the principles inherent in the sliding scale arrangement, on which, as heretofore stated, the credit position of the Company depends in large measure" (R. I, 51, 52). The Commission also said (*id.* 50–51):

> On January 17, 1941, the Company filed an application with this Commission for authority to increase its capitalization by 90,000 shares of $4.25 preferred stock. Due principally to the lack of a quorum on the Commission this application was not acted upon until March 26, 1942 (Order No. 2221). At that time, *due to depressed market conditions,* the Company was unable to sell this newly created stock and endeavored to sell 40,000 shares of its $5.00 cumulative preferred stock with the result heretofore stated. [Italics added.]

While the Commission noted that "depressed market conditions" had prevented the sale of the

proposed preferred stock issue, it assumed that these conditions could be overcome by a rate increase. It ignored the fact that these conditions were not caused by the temporary decline in the company's net income after war taxes (due perhaps as much to the temporary weather factor as to any other), but by prevailing war conditions over which neither the Commission nor the company had any substantial control. It is a well recognized fact, shown by the decline in the market price of securities, both equity stocks and bonds, in the spring and summer of 1942, that this decline was the result of the unfavorable war situation. Had the Commission undertaken to determine whether a rate increase was necessary to permit needed financing, surely it would have sought evidence as to financial market prospects generally, as to the effect, if any, of a denial of the rate increase on the Company's prospects as the market became more normal, and whether an offering on more favorable terms was indicated. Far from obtaining proof of necessity, the Commission majority simply concluded that it would be advisable to cast the burden of a rate increase on the rate payers on the chance that the increase would be helpful to the financing prospects of a company which enjoyed an extraordinary record of prosperity (R. II, 421–422). It would indeed be a dangerous principle of utility rate making for regulatory commissions to assume that increases in utility

rates could overcome temporary adverse market conditions.

That there was no genuine relationship between the rate increase and the ability of the company to market its securities was soon confirmed. On February 18th, *after* the Commission's order authorizing the increase was set aside by the District Court, the company sold $4,750,000 of 3¾% refunding mortgage bonds. This sale was characterized by the Commission in a later proceeding as "advantageous refinancing." Opinion in Formal Case No. 334, P. U. C. No. 3361, Nov. 8, 1943, at p. 10.

The Commission also justified the rate increase by a reference to the decline in the company's earnings (R. I, 51). As we have pointed out, *supra,* pp. 49–50, the Commission's conclusions as to the earnings of the company [42] ignored the temporary decline of revenues due to the abnormally light winter and also ignored the fact that the revenues for the first seven months of 1942 enabled the company to absorb all increased costs including increased wages with the exception of part of the higher federal income taxes estimated payable under the 1942 revenue act (R. II, 383; Tr. 827–828).

The Commission's conclusion that a wartime in-

[42] The earning figures were applicable to the Company's entire operations including those in Maryland and Virginia. What part of the decline was due to those operations was not considered by the Commission.

crease could be justified because the credit position of the company "depends in large measure upon the integrity of the Commission, in administering the sliding-scale arrangement" means little more than that the maintenance of peacetime profits of the investors is at least as important as the requirement that the company assume a part of the burdens of the war by foregoing a rate increase. Perhaps the Commission felt that unless the investors and the company could be assured of such profits, they would go on a sit-down strike.

Not abandonment, but only a wartime adjustment in the arrangement was here in prospect. A more realistic approach to the financial position of the company would have demonstrated that its real strength lay less in the arrangement, which began in 1935, than in the monopoly of the company in rendering gas service in a territory which has produced extraordinary profits throughout its history, including the depression periods.

The significant financial history of the company, ignored by the Commission, disclosed that in 1931, the worst year of the depression, the company earned 10.6% upon a base of 18½ million dollars, as compared with the 21-million-dollar rate base fixed in the sliding-scale arrangement (R. II, 422). Between 1927 and 1934 it earned an average return of 9.2% on the average capital employed in its business after the deduction of federal income

taxes (*Ibid,*). Between 1936 and 1941, under the arrangement, it earned an average return of 6.86 (R. II, 421), upon an undepreciated rate base. It is true that the company made reductions in rates totalling approximately $328,000 during the period, but the company was also permitted under the sliding-scale arrangement to retain one-half of the earnings in excess of 6½% in the same amount. Moreover, the depreciation reserve has increased from $879,289 as of December 31, 1936, to $2,171,608 on December 31, 1941 (R. II, 421). The earned surplus of the company had increased from $5,398,927 as of December 31, 1936, to $6,271,626 as of December 31, 1941 (*Ibid.*). That the company's depreciation reserve and surplus had grown substantially in recent years seems not to have been understood by the court below (R. II, 439).[43]

Further scrutiny of the rate increase order in relation to the ability of the company to maintain its credit or market its securities discloses little if any relationship between the two. The company, if it became subject to excess profits taxes as a result of the rate increase, became obli-

[43] The Commission might also have officially noticed the following pertinent facts in connection with the financial history of the Company:

1. Of the total common stock in the amount of $3,650,000 only $2,550,000 has been paid in by stockholders in money or property on which $1,050,000 was paid in 1939 (P. U. C.

gated under the provisions of the order to refund the additional revenues (R. I, 49). The company has already refunded such additional revenues for 1942 (Brief of Public Utilities Commission in opposition to certiorari, p. 9, n. 4). Even if it will not be required to refund additional revenues for 1943, its liability for federal and state taxes on the additional income will leave the company only about half the increased revenues. If a rate increase bore a substantial relationship to the ability of the company to sell securities, the Commission, it would seem, should have given the company an increase amounting to many times that granted by the Order of October 13. These implications of respondents' argument repel its acceptance.

Order No. 1341, March 19, 1935 (Tr. 128–129), pp. 1, 2; Order #2682, p. 36, n, 46, November 8, 1943).

2. In 1874, the extra cash dividend was one of 50%, or $750,000 on the then $1,500,000 of outstanding stock. This dividend was repeated in 1876, and, in 1883, one of 40% or about $800,000 was paid. In 1891 the extra payment amounted to $600,000, and in 1893 and 1895 a total of $700,000 extra was disbursed. The total of extra cash dividends was $3,600,000. (P. U. C. Order No. 209, pp. 9–12, May 2, 1917.)

3. The common stockholders also received $2,600,000 in gold bonds as a bonus. (P. U. C. Order No. 209, p. 13; Order #1341, March 19, 1935 (Tr. 128), p. 1; Order #2682, Nov. 8, 1943, p. 36, n. 46).

4. From 1865 through 1908 regular dividends on the common stock averaged 10%; in 1909 they were 20%, in 1910, 15%; 1911 through 1916, 24%; in 1917, 22½%; 1918 through 1933, 18%; in 1934, 22½%; 1935 through 1937, 18%; in 1938, 19½%; in 1939 (on the basis of $3,650,000 capital stock) 16¾%; 1940 through 1942 (on the same basis) 18%. The total was $30,317,500. (Order #209, *supra*, p. 11; Order #1341, *supra*, p. 1; Order #2682, *loc. cit. supra*).

C. THE MERE DISALLOWANCE BY THE COMMISSION AS AN IMPROPER OPERATING EXPENSE OF INCOME TAXES COMPUTED AT CORPORATE INCOME TAX RATES ABOVE THOSE IN EFFECT FOR 1941 DID NOT JUSTIFY THE INCREASE, OR CONSTITUTE GIVING ADEQUATE EFFECT TO THE STABILIZATION PROGRAM

To give due consideration to the effect of wartime taxes in passing upon the right of a utility to increase rates during the war, the Commission should have either (1) reconsidered the rate of return in the light of the stabilization legislation and the changed economic conditions, recognizing the absorption by the customers of the wartime taxes of the company if allowed as an operating cost, or (2) disallowed all war and emergency federal income taxes as an operating cost. A somewhat higher rate of return would probably be justified in the latter than in the former case. As we have demonstrated, the Commission refused to reopen the question of rate of return. Had it done so, it could have considered the effect of the allowance of war emergency taxes as an operating expense. Instead of adopting the course suggested by the Administrator and Director, the Commission held that it would give adequate effect to the government's wartime program to keep down the cost of living by excluding as an operating cost all excess profits taxes, and income taxes of the company over and above those based on the Revenue Act of 1941 (which established a corporate tax rate of 31%). The Court of Appeals apparently concluded that the Commission thereby demonstrated

that it was not "oblivious to the economic conditions consequent upon the war and did not disregard them in formulating its findings and opinion" (R. II, 435).

To the extent that federal income taxes constitute an element of allowable operating expense, the commission should not have allowed income taxes in excess of those based upon the highest corporate tax rate which prevailed through the 1936–1939 period, or 19%. This, as we shall show, was the maximum allowance that should have been made in order that the company might bear its proportionate part of the burdens of the war and in order that unfair treatment of the company's consumers might be avoided.

It is clear that all revenue acts adopted by Congress since 1939 have been heavily weighted by the extraordinary expenditures incurred for the defense of the nation. The reports of the Committee on Ways and Means of the House of Representatives relating to each of the revenue acts from 1939 to 1943, inclusive, demonstrate that the proper line between emergency and prewar taxes is in 1939 and not 1941 as held by the Commission. In recommending the 1940 Revenue Bill, which provided for an increase in the rates from 19% to 24%, the Committee stated: [44]

> The Committee on Ways and Means, to whom was referred the bill [the Revenue

[44] Report No. 2491, 76th Congress, 3rd Sess., H. R. 10039 (Rev. Bill of 1940, p. 1–3).

Bill of 1940] to provide for the expenses of national preparedness by raising revenue and issuing bonds, * * *

* * * * * * *

* * * It is the desire of this committee, which is favorably reporting a bill which will enable a larger proportion of our citizens to participate in the responsibility of providing an adequate national defense than has ever been the case before, that there shall not be an opportunity for the creation of new war millionaires or the further substantial enrichment of already wealthy persons because of the rearmament program.

Congress thereby definitely expressed its intention that all citizens and corporations should assume their proportionate financial responsibility for providing for the national defense. The passing on of war and emergency taxes to utility consumers means that the consumers and not the utility would assume such taxes. And the Ways and Means Committee stated with respect to the 1941 revenue act:[45]

> The bill is unprecedented in the amount of revenue it is designed to provide. It lays a substantially increased burden upon the American people. But there is convincing evidence that this burden will be borne cheerfully in the light of the overwhelming importance of national defense to the contin-

[45] Report No. 1040, 77th Congress, 1st Sess., H. R. 5417 (Rev. Bill of 1941, p. 1-2).

> ued freedom and security of the United States. * * *
>
> In its deliberations on this measure, it has been your committee's aim and desire to distribute the additional tax burden as equitably as possible among the several classes of taxpayers.

It is clear that the 1940 and 1941 Revenue Acts providing for higher tax rates were enacted as a result of the greatly increasing expenditures arising out of the war. On the other hand, the national emergency did not affect the provisions of the 1939 Bill.[46]

The inflationary character of allowing federal income taxes as an operating expense was clearly demonstrated by the Price Administrator's witness Riley (R. I, 151) who testified that it was the practice of the Administrator to consider profits before federal income taxes in determining the reasonableness of maximum prices under the stabilization legislation. In his testimony, he asserted (R. I, 155):

> In the case of income taxes and excess-profits taxes, the Congressional intent is the reverse; by their very nature they are in-

[46] "The bill has two major objectives. The first is to remove from the existing corporate income-tax structure such business deterrents and tax irritants as may be possible to consider at this time. Its second purpose is to extend the temporary excise taxes and postal rates." (Report No. 855, 76th Congress, 1st Session, H. R. 6851 (Revenue Bill of 1939, pp. 1–2).)

tended to be paid by the person to whom they are assessed and not to be passed on through higher prices. To include them in cost would place the Price Administrator or any other agency or price or rate control in the impossible position of sanctioning an increase of prices whenever the burden of taxation was increased. No more deliberately inflationary policy could be adopted.

The policy of including income taxes in business costs would have serious effects going far beyond the direct raising of prices. If corporate incomes are to be increased by the amount of additional taxes, individual incomes should be accorded the same treatment. Business and government salaries should be increased by the amount of additional income taxes. The War Labor Board formula should be amended to provide that wages shall rise to cover the workers' additional income taxes! We should all share in the remarkable privilege of passing on our war taxes to others![47]

Moreover, in determining costs under wartime contracts, the War and Navy Department instructions provide:

Among the items which shall be excluded as a part of the cost of performing a con-

[47] This position is strongly corroborated in a letter of Chairman Ayres of the Federal Trade Commission, dated September 15, 1942, stating that the practice of including income taxes in costs would "set up a vicious spiral", and calling attention to its "inflationary character". 88 Cong. Rec. 7634–7635 (September 30, 1942).

> tract or subcontract, or considered in determining such costs, are the following: * * * Federal and State income and excess-profits taxes and surtaxes; * * * (Treasury Decision 5000, § 26.9 (g) (4), 5 F. R. (1940) 2793)."[48]

Likewise, the general commercial practice is not to consider income taxes as an element of cost in the determination of the cost of production."[49]

It is true that this Court held in *Galveston Electric Co.* v. *Galveston,* 258 U. S. 388, that federal income taxes are properly chargeable as an operating expense for a public utility in determining the issue of confiscation. But this decision should not be construed as imposing an obligation upon state and federal utility agencies to require consumers of utilities to absorb the war taxes of the utility industry. The Revenue Act under consideration there provided for but a 10% tax rate in contrast with the current corporate normal and surtax rates in the amount of 40% and 90% excess-profits taxes. We submit that the *Galveston* decision properly construed should not permit

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[48] Explanation of Principles for Determination of Costs under Government Contracts, War Dept.–Navy Dept. U. S. Govt. Printing Office, April 1942, p. 15.

[49] National Association of Cost Accountants Year Book. 1939, Proceedings of the Twentieth International Cost Conference; George E. Bennett, *Accounting Principles and Practices*, p. 185.

the inclusion of an operating cost of more than the usual ordinary income taxes.

Moreover, the Court there recognized that the position of the stockholders must be looked to, and hence concluded that the advantageous tax-exempt treatment of dividends received by the stockholders must be taken into account in appraising a fair rate of return. By the same token, the position of the stockholders in relation to the sharing of wartime tax burdens must be considered in the allocation of wartime taxes for rate-making purposes, and particularly in the assessment of a fair rate of return. This analysis has been well developed in a recent statement by Chairman Clyde O. Fisher of the Connecticut Commission who, though approving the allowance of all taxes as an operating expense, suggested that under present conditions the allowance of a rate of return of 4% would constitute the assumption of an appropriate share of the war burden by a utility. In his statement he asserted:

> It follows from this that it would be entirely appropriate to recast our thinking as to what constitutes a fair rate of return. The utility companies should have no cause for complaint if earnings were so reduced as to constitute a constant share of the total purchasing power used for nonwar purposes. Perhaps, under present conditions, a rate of 4% after all expenses including taxes is as high, comparatively and rela-

tively speaking, as would have been a rate of six or seven percent in the pre-war era. You will recall that Mr. Justice Brandeis in 1922 said that the exemption of dividends from the income tax constituted in reality a portion of the so-called fair rate of return. By the same token the assumption of one's appropriate share of the war burden might easily result in a reduction of what we have thought of traditionally as a fair rate of return. The solution of the problem that seems most promising was illustrated by a statement of the Bridgeport Hydraulic Company of Bridgeport, Connecticut, in notifying its stockholders in September 1942 of a reduction of 25% in the dividend rate: "to make a long story short, we are in the midst of the worst war in all history, and the company and its stockholders are a part of it" [50]

As the Commission restricted the hearing so as to preclude the reexamination of rate of return in the light of wartime economic conditions, and allowed the utility a rate increase when it was earning 5% upon an undepreciated rate base, with every prospect of improvement in income, it did not in merely disallowing income taxes above the rate of 31% thereby give such effect to wartime conditions as to justify its rate increase order.

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[50] Clyde O. Fisher, *The Incidence of War Taxes: Should They be Approved Operating Expenses*, War Convention of the National Association of Railroad & Utilities Commissioners, Sept. 15, 1943.

CONCLUSION

For the foregoing reasons the judgment of the court below should be reversed with directions either to remand the case to the Commission for further proceedings or to vacate and set aside the order of the Commission.

Respectfully submitted.

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JANUARY 1944.

APPENDIX

The Emergency Price Control Act of 1942, 56 Stat. 23:

Sec. 1 (a) (50 U. S. C. App., Supp. II, § 901 (a)):

> It is hereby declared to be in the interest of the national defense and security and necessary to the effective prosecution of the present war, and the purposes of this Act are, to stabilize prices and to prevent speculative, unwarranted, and abnormal increases in prices and rents; to eliminate and prevent profiteering, hoarding, manipulation, speculation, and other disruptive practices resulting from abnormal market conditions or scarcities caused by or contributing to the national emergency; to assure that defense appropriations are not dissipated by excessive prices; to protect persons with relatively fixed and limited incomes, consumers, wage earners, investors, and persons dependent on life insurance, annuities, and pensions, from undue impairment of their standard of living; to prevent hardships to persons engaged in business, to schools, universities, and other institutions, and to the Federal, State, and local governments, which would result from abnormal increases in prices; to assist in securing adequate production of commodities and facilities; to prevent a post emergency collapse of values; to stabilize agricultural prices in the manner provided in section 3; and to permit voluntary coopera-

tion between the Government and producers, processors, and others to accomplish the aforesaid purposes. * * *

Sec. 302 (c) (50 U. S. C. App., Supp. II, § 942 (c)):

* * * *Provided,* That nothing in this Act shall be construed to authorize the regulation of (1) compensation paid by an employer to any of his employees, or (2) rates charged by any common carrier or other public utility * * *.

Act of October 2, 1942, c. 578, 56 Stat. 765:

That in order to aid in the effective prosecution of the war, the President is authorized and directed, on or before November 1, 1942, to issue a general order stabilizing prices, wages, and salaries, affecting the cost of living; and, except as otherwise provided in this Act, such stabilization shall so far as practicable be on the basis of the levels which existed on September 15, 1942. The President may, except as otherwise provided in this Act, thereafter provide for making adjustments with respect to prices, wages, and salaries, to the extent that he finds necessary to aid in the effective prosecution of the war or to correct gross inequities: *Provided,* That no common carrier or other public utility shall make any general increase in its rates or charges which were in effect on September 15, 1942, unless it first gives thirty days notice to the President, or such agency as he may designate, and consents to the timely intervention by such agency before the Federal, State, or municipal authority having jurisdiction to consider such increase.

Sec. 2:

The President may, from time to time, promulgate such regulations as may be necessary and proper to carry out any of the provisions of this Act; and may exercise any power or authority conferred upon him by this Act through such department, agency, or officer as he shall direct. The President may suspend the provisions of sections 3 (a) and 3 (c), and clause (1) of section 302 (c), of the Emergency Price Control Act of 1942 to the extent that such sections are inconsistent with the provisions of this Act, but he may not under the authority of this Act suspend any other law or part thereof.

* * * * *

Sec. 7:

* * * * *

(c) Nothing in this Act shall be construed to invalidate any provision of the Emergency Price Control Act of 1942 (except to the extent that such provisions are suspended under authority of section 2), or to invalidate any regulations, price schedule, or order issued or effective under this Act.

Executive Order No. 9250 (7 Fed. Reg. 7871):

By virtue of the authority vested in me by the Constitution and the Statutes, and particularly by the Act of October 2, 1942, entitled "An Act to Amend the Emergency Price Control Act of 1942, to aid in Preventing Inflation, and for Other Purposes," as President of the United States and Commander in Chief of the Army and Navy, and in order to control so far as possible the inflationary tendencies and the vast dis-

locations attendant thereon which threaten our military effort and our domestic economic structure, and for the more effective prosecution of the war, it is hereby ordered as follows:

Title I—Establishment of an office of economic stabilization:

* * * * *

4. The guiding policy of the Director and of all departments and agencies of the Government shall be to stabilize the cost of living in accordance with the Act of October 2, 1942; and it shall be the duty and responsibility of the Director and of all departments and agencies of the Government to cooperate in the execution of such administrative programs and in the development of such legislative programs as may be necessary to that end. The administration of activities related to the national economic policy shall remain with the departments and agencies now responsible for such activities, but such administration shall conform to the directives on policy issued by the Director.

* * * * * *

Id., Title VI—General Provisions:

4. The Director shall be the agency to receive notice of any increase in the rates or charges of common carriers or other public utilities as provided in the aforesaid Act of October 2, 1942.

Executive Order No. 9328, par. 4 (8 Fed. Reg. 4681, 4682):

The attention of all agencies of the Federal Government, and of all State and municipal authorities, concerned with the

rates of common carriers or other public utilities, is directed to the stabilization program of which this order is a part so that rate increases will be disapproved and rate reductions effected, consistently with the Act of October 2, 1942, and other applicable federal, state, or municipal law in order to keep down the cost of living and effectuate the purposes of the stabilization program.

District of Columbia Code (1940 ed.)

Section 43–301:

Every public utility doing business within the District of Columbia is required to furnish service and facilities reasonably safe and adequate and in all respects just and reasonable. The charge made by any such public utility for any facility or services furnished, or rendered, or to be furnished or rendered, shall be reasonable, just, and nondiscriminatory. Every unjust or unreasonable or discriminatory charge for such facility or service is prohibited and is hereby declared unlawful. Every public utility is hereby required to obey the lawful orders of the commission created by chapters 1–10 of this title (Mar. 4, 1913, 37 Stat. 977, ch. 150, § 8, par. 2).

Section 43–306:

The commission shall value the property of every public utility within the District of Columbia actually used and useful for the convenience of the public at the fair value thereof at the time of said valuation (Mar. 4, 1913, 37 Stat. 978, ch. 150, § 8, par. 7).

Section 43–315:

Every public utility shall carry a proper and adequate depreciation account. The

Commission shall ascertain and determine what are the proper and adequate rates of depreciation of the several classes of property of each public utility. These rates shall be such as will provide the amounts required over and above the expense of maintenance to keep such property in a state of efficiency corresponding to the progress of the industry. Each public utility shall conform its depreciation accounts to such rates so ascertained and determined by the commission. The commission may make changes in such rates of depreciation from time to time as it may find to be necessary. The commission shall also prescribe rules, regulations, and forms of accounts regarding such depreciation which the public utility is required to carry into effect. The commission shall provide for such depreciation in fixing the rates, tolls, and charges to be paid by the public. All moneys in this fund may be expended in keeping the property of such public utility in repair and good and serviceable condition for the use to which it is devoted, or invested, and, if invested, the income from the investments shall also be carried in the depreciation fund. This fund and the proceeds thereof shall be used for no other purpose than as provided in this section, unless with the consent and by order the commission (Mar. 4, 1913, 37 Stat. 979, ch. 150, § 8, par. 16).

Section 43–317:

Nothing in chapters 1–10 of this title shall be taken to prohibit a public utility, with the consent of the commission, from providing a sliding scale of rates and dividends according to what is commonly known as the Boston sliding scale, or other financial device that may be practicable

and advantageous to the parties interested. No such arrangement or device shall be lawful until it shall be found by the commission, after investigation, to be reasonable and just and not inconsistent with the purposes of chapters 1–10 of this title. Such arrangement shall be under the supervision and regulation of the commission. The commission shall ascertain, determine, and order such rates, charges, and regulations, and the duration thereof, as may be necessary to give effect to such arrangement, but the right and power to make such other and further changes in rates, charges, and regulations as the commission may ascertain and determine to be necessary and reasonable, and the right to alter or amend all orders relative thereto, is reserved and vested in the commission notwithstanding any such arrangement and mutual agreement (Mar. 4, 1913, 37 Stat. 980, ch. 150, § 8, par. 18).

Section 43–402:

The commission shall have power to adopt reasonable and proper rules and regulations relative to all inspections, tests, audits, and investigations, and to adopt and publish reasonable and proper rules to govern its proceedings and to regulate the mode and manner of all investigations and hearings of public utilities and other parties before it (Mar. 4, 1913, 37 Stat. 982, ch. 150, §8, par. 32).

Section 43–411:

If upon such investigation the rates, tolls, charges, schedules, or joint rates shall be found to be unjust, unreasonable, insufficient, or unjustly discriminatory, or to be

preferential or otherwise in violation of any of the provisions of chapters 1–10 of this title, the commission shall have power to determine and by order fix and order to be substituted therefor such rate or rates, tolls, charges, or schedules as shall be just and reasonable. If upon such investigation it shall be found that any regulation, time schedule, act, or service complained of is unjust, unreasonable, insufficient, preferential, unjustly discriminatory, or otherwise in violation of any of the provisions of this section, or if it is to be found that reasonable service is not supplied, the commission shall have power to determine and substitute therefor such other regulations, time schedules, service, or acts, and to make such orders respecting and such changes in such regulation, time schedules, service, or acts as shall be just and reasonable. And upon any investigation for the purpose of determining upon and requiring any reasonable extension or extensions of lines or of service that shall promise to be compensatory within a reasonable time, the commission shall have power to fix, determine, and require every such extension or extensions to be made and the terms and conditions upon which the same shall be made: *Provided,* That no hearing shall be had and no order shall be made respecting such extension or extensions, without notice to the public utility affected thereby, as provided in section 43–410 (Mar. 4, 1913, 37 Stat. 983, ch. 150, § 8, par. 41).

Section 43–705:

The District Court of the United States for the District of Columbia shall have jurisdiction to hear and determine any appeal from an order or decision of the Commission. Any public utility or any other

person or corporation affected by any final order or decision of the Commission, other than an order fixing or determining the value of the property of a public utility in a proceeding solely for the purpose, may, within sixty days after final action by the Commission upon the petition for reconsideration, file with the clerk of the District Court of the United States for the District of Columbia a petition of appeal setting forth the reasons for such appeal and the relief sought; at the same time such appellant shall file with the Commission notice in writing of the appeal together with a copy of the petition. Within twenty days of the receipt of such notice of appeal the Commission shall file with the clerk of the said court the record, including a transcript of all proceedings had and testimony taken before the Commission, duly certified, upon which the said order or decision of the Commission was based, together with a statement of its findings of fact and conclusions upon the said record, and a copy of the application for reconsideration and the orders entered thereon: * * * Any such appeal shall be heard upon the record before the Commission, and no new or additional evidence shall be received by the said court. The said court, or any justice or justices thereof, before whom any such appeal shall be heard, may require and direct the Commission to receive additional evidence upon any subject related to the issues on said appeal concerning which evidence was improperly excluded in the hearing before the Commission or upon which the record may contain no substantial evidence. Upon receipt of such requirement and direction the Commission shall receive such evidence and

without unreasonable delay shall transmit to the said court the findings of fact made thereon by the Commission and the conclusions of the Commission upon the said facts.

Upon the conclusion of its hearing of any such appeal, the court shall either dismiss the said appeal and affirm the order or decision of the Commission or sustain the appeal and vacate the Commission's order or decision. In either event the court shall accompany its order by a statement of its reasons for its action, and in the case of the vacation of an order or decision of the Commission the statement shall relate the particulars in and the extent to which such order or decision was defective.

Any party, including said Commission, may appeal from the order or decree of said court to the United States Court of Appeals for the District of Columbia, which shall thereupon have and take jurisdiction in every such appeal. Thereafter the Supreme Court of the United States may, upon a petition for certiorari granted in its discretion, review the said case * * * (Mar. 4, 1913, 37 Stat. 989, ch. 150, § 8, par. 65; Aug. 27, 1935, 49 Stat. 882, ch. 742, § 2).

Section 43–706:

In the determination of any appeal from an order or decision of the Commission the review by the court shall be limited to questions of law, including constitutional questions; and the findings of fact by the Commission shall be conclusive unless it shall appear that such findings of the Commission are unreasonable, arbitrary, or capricious (Mar. 4, 1913, 37 Stat. 989, ch. 150, § 8, par. 66; Aug. 27, 1935, 49 Stat. 883, ch. 742, § 2).

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Section 43–911:

Whenever, after hearing and investigation as provided in chapters 1–10 of this title, the commission shall find that any rate, toll, charge, regulation, or practice of any public utility within the District of Columbia is unreasonable or discriminatory, it shall have the power to regulate, fix, and determine the same as provided in chapters 1–10 of this title (Mar. 4, 1913, 37 Stat. 992, ch. 150, § 8, par. 88).

Section 43–1002:

The Commission shall inquire into any neglect or violation of the laws or regulations in force in the District of Columbia by any public utility doing business therein, or by the officers, agents, or employees thereof, or by any person operating the plant of any public utility, and shall have the power, and it shall be its duty, to enforce the provisions of chapters 1–10 of this title as well as all other laws relating to public utilities (Mar. 4, 1913, 37 Stat. 993, ch. 150, § 8, par. 90).

Section 43–201:

The Public Utilities Commission of the District of Columbia shall be composed of three commissioners as follows: (1) The Engineer Commissioner of the District of Columbia, and (2) two persons appointed by the President, by and with the advice and consent of the Senate * * * (Dec. 15, 1926, 44 Stat. 920, ch. 8, § 1).

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